Technical Bulletin 2020/1

Technical developments and emerging risks from January to March 2020

AUDIT SCOTLAND

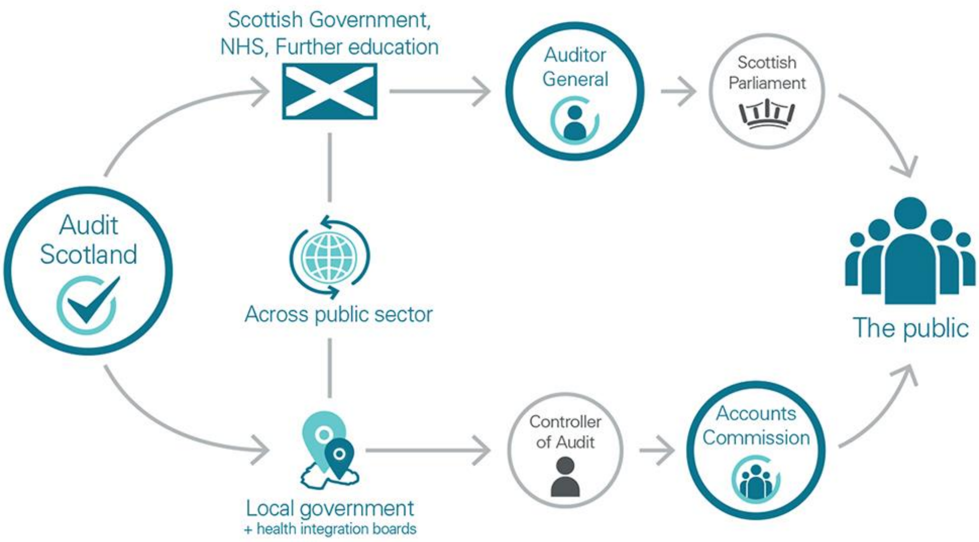
Prepared for appointed auditors and audited bodies in all sectors

31 March 2020

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

Contents

Introduction

Purpose

1. The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:
   - information on the main technical developments in each sector and on professional matters during the quarter
   - guidance on any emerging risks identified in the quarter.
2. Appointed auditors are required to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require to be aware of. It may still be necessary for auditors to read the source material if greater detail is required. These can be accessed by using the hyperlinks. They are also available from the Technical Reference Library maintained by Professional Support.

Technical Bulletins provide information on developments and guidance on emerging risks

3. The actions by auditors recommended by Professional Support in respect of each item are highlighted in red and are also summarised at the end of each section.
4. Technical Bulletins are also published on the Audit Scotland website and therefore are available to audited bodies and other stakeholders. Hyperlinks indicated with an asterisk link to the Technical Reference Library and therefore are active only for auditors.

Highlights summary

5. Particular attention is drawn in the following table to fifteen items in this Technical Bulletin:

Highlights summary		
The Financial Reporting Council has issued guidance on issues arising from the COVID-19 pandemic [see paragraph 8]	Professional Support has published guidance for auditors on dealing with statutory objections to the unaudited 2019/20 local government annual accounts [see paragraph 14]	Professional Support has published a protocol for audit assurances in respect of the Local Government Pension Scheme [see paragraph 15]
CIPFA has issued guidance on IFRS 16 in local government [see paragraph 20]	CIPFA has issued a briefing on accounting for the McCloud and Sargeant judgements in 2019/20 [see paragraph 25]	Professional Support has published a Good Practice Note on Management Commentaries [see paragraph 30]
Professional Support has published guidance on risks of misstatement in 2019/20 annual report accounts of central government bodies [see paragraph 35]	Treasury has issued the 2019/20 and 2020/21 editions of the FReM [see paragraphs 41 and 43 respectively]	Professional Support has published 2019/20 model Independent Auditor's Report for health boards [see paragraph 68]

Highlights summary		
The Scottish Government has issued the 2019/20 accounts manual for health boards [see paragraph 74]	The Technical Accounting Group has issued guidance on applying IFRS 15 to research and development contracts [see paragraph 78].	The Financial Reporting Council has issued a number of revised auditing standards [see paragraph 83]
The Financial Reporting Council has issued an exposure draft of proposed revisions to ISA (UK) 315 on auditing estimates [see paragraph 84]	The Bryden Review has issued a report on the quality and effectiveness of audit [see paragraph 87]	The International Accounting Standards Board has issued an exposure draft on improving the presentation of and disclosures in the financial statements [see paragraph 88]

Impact of COVID 19

6. This bulletin refers to some developments that relate specifically to the COVID 19 pandemic. However, COVID 19 has the potential to impact on many of the items included in this bulletin, particularly any dates referred to. While information is correct at the time of publication on 31 March 2020, all items may therefore be subject to change in due course, including changes arising from the forthcoming Coronavirus (Scotland) Act 2020 and proposals around local government annual accounts.

Contact point

7. The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – pobrien@audit-scotland.gov.uk.

Feedback on this Technical Bulletin is welcome

Section 1

Cross sector

COVID-19-related accounting and auditing guidance

8. The Financial Reporting Council (FRC) has issued guidance for both auditors and preparers of financial statements on issues arising from the COVID-19 pandemic.

9. Initial audit guidance acknowledged the practical difficulties in preparing financial statements and carrying out audits, and the need for auditors to develop alternative audit procedures to gather sufficient, appropriate audit evidence. However, the guidance is clear that this should not undermine the delivery of high quality audits, which should continue to comply fully with international standards on auditing. Where additional time is required to complete audits, it is important that this is taken even at the risk of not meeting deadlines.

Auditors should continue to comply fully with required standards

10. The FRC followed up that initial guidance with a bulletin that provides a list of factors auditors should be considering when carrying out audits in the current circumstances, along with guidance on how they might be addressed. Some key points raised in the bulletin are as follows:

- The impact of COVID-19 is likely to require auditors to revisit their risk assessment and the proposed response to identified risks. In particular, auditors should consider whether their assessment of risks of material misstatement due to fraud or irregularity needs to be heightened.
- Auditors will need to agree with audit committees how to communicate with them through means other than physical meetings.
- Given restrictions on travel, movement and visiting sites, auditors will need to think about whether there are other ways for them to obtain sufficient, appropriate audit evidence, including greater use of technology.
- Auditors' assessment of the sufficiency and appropriateness of audit evidence should be clearly documented on the file. The assessment should recognise how the auditor addresses any risk that the quality and reliability of such evidence may be lower, for example through more directed testing of items.

Factors for auditors to consider

- Auditors should identify those items where the verification of original source documentation or physical assets are absolutely vital.
- The current circumstances may lead to more modified opinions in the Independent Auditor's Report. This may be where sufficient appropriate audit evidence cannot be obtained or due to the existence of material misstatements caused by, for example, the failure to recognise the impairment of assets or adequate provisions for obligations, or to provide related disclosures.
- Where auditors intend to modify their opinion, they should engage with audit committees to explain whether the nature of the modification may be ameliorated by allowing the auditor additional time to undertake their work, and obtain the evidence required.
- Auditors will need to consider how they demonstrate and record an appropriate level of professional scepticism to reflect that audits may be delivered in a different way.

11. The FRC has also issued guidance aimed at the boards of entities on disclosing risks and uncertainties related to COVID 19, as well as further guidance on corporate governance and reporting in an environment impacted by COVID 19 which:

- highlights some key areas of focus in maintaining strong corporate governance
- provides high-level guidance on some of the most pervasive issues when preparing the annual report and other corporate reporting.

12. The guidance highlights that the need for clear leadership, robust governance and effective decision making based on reliable information is stronger than ever. It advises boards to develop and implement mitigating actions and processes to ensure that they continue to operate an effective control environment. This should address key reporting and other controls on which entities have placed reliance historically, but which may not prove effective in the current circumstances.

The need for robust governance is stronger than ever

13. The guidance in respect of corporate reporting covers:

- the need for narrative reporting to provide forward-looking information that is specific to the entity
- the increased importance of providing information on significant judgements applied in the preparation of the financial statements, sources of estimation uncertainty and other assumptions made
- the judgement required in determining the appropriate reporting response to events after the reporting date and the extent to which qualitative or quantitative disclosures may be appropriate.

Section 2
Local government sector

Auditing developments

Technical Guidance Note on statutory objections in 2019/20

14. Professional Support has published Technical Guidance Note (TGN) 2020/3(LG)* to provide auditors with guidance on dealing with statutory objections to the unaudited 2019/20 local government annual accounts.

Auditor action
Auditors should pay due regard to TGN 2020/3(LG)

Assurance protocol on LGPS

15. Professional Support has published a protocol* which provides an agreed framework for:

- Local Government Pension Scheme (LGPS) pension fund auditors to request assurances from employer body auditors in respect of pension contributions payable by the employer body to the pension fund
- employer body auditors to request assurances from pension fund auditors in respect of information provided by the pension fund to the actuary in relation to their reports on employer bodies.

16. Auditors may judge that it is not necessary to request any assurances from other auditors. However, where assurances are judged to be appropriate, this protocol sets out the potential range of assurances.

Financial statements developments

Suspension of 2019/20 accounting code

17. The Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chair of the CIPFA/LASAAC Local Authority Code Board have issued a joint statement on proposals to replace the 2019/20 Code of Practice on Local Authority Accounting in the UK (accounting code) with a simplified version in order the ease the burden as local authorities respond to the impact of COVID-19.

Proposal to replace 2019/20 accounting code with a simplified version

18. The proposal is to be discussed by CIPFA/LASAAC in early April. Professional Support will advise auditors of the outcome of the discussions in due course. Even if agreed, any change would be subject to approval from the Financial Reporting Advisory Board and other stakeholders.

Guidance on leases under IFRS 16

19. CIPFA has issued IFRS 16 An Early Guide for Local Authority Practitioners* to provide guidance on how the provisions of IFRS 16 Leases are expected to apply in local government. The guide covers requirement in respect of:

- the identification of leases
- the recognition of right-of-use assets and liabilities and their subsequent measurement
- treatment of gains and losses
- derecognition and presentation and disclosure in the financial statements
- the management of leases within the Prudential Framework.

20. The guide also covers the transitional arrangements for moving to these new requirements, such as:

- the recognition of right-of-use assets and liabilities for leases previously accounted for as operating leases by lessees

- the mechanics of making the transition, including the application of transitional provisions and the preparation of relevant disclosure notes.

Draft revised statutory guidance on financial instruments

Capital receipts held in the Capital Fund cannot be used to fund premiums

21. The Scottish Government has issued a consultation draft* of proposed revisions to the statutory guidance on financial instruments. The proposed revisions, currently intended to apply from 2019/20, relate to the use of capital receipts to fund premiums incurred on the early repayment of debt.

22. As capital receipts held in the Capital Fund (or Capital Receipts Reserve) cannot be used to fund the cost of premiums, it is proposed that capital receipts that are to be used in that way should be:

- credited directly to the Capital Grants and Receipts Unapplied Account as a statutory adjustment
- transferred from the Capital Grants and Receipts Unapplied Account to the General Fund as a movement in reserves.

23. Capital receipts may be used to fund the cost of premiums as they are incurred or to fund the annual charge for those premiums that have been deferred and held in the Financial Instruments Adjustments Account (FIAA). The draft guidance therefore sets out four possible scenarios, depending on whether:

- the local authority wants to fund the premium when incurred or the annual charge
- the receipt will be applied in the year received or set aside.

24. The four scenarios, and the particular requirements applying to each, are summarised in the following table:

Fund	Capital receipt	Requirements
Annual charge	Received in year	The value of the capital receipt transferred cannot be more than the annual charge to be funded
	Set aside	Additional charges require to be made equal to the capital receipt being set aside for that use, and the schedule of annual charges adjusted accordingly
Premium when incurred	Received in year	The value of the capital receipt transferred cannot be more than the premium to be funded
	Set aside	This option is available only if there are no deferred premiums held in the FIAA

Bulletin on accounting for McCloud judgement

IAS 19 liability should take into account the expected impact of the judgements.

25. CIPFA has issued a briefing on accounting for the McCloud and Sargeant judgements (the judgements) in 2019/20.

26. The briefing advises that the announcement in July 2019 by the Treasury that the judgements would apply to all public service pension schemes confirms that the judgements create a legal obligation for the LGPS. All members of the schemes who fell outside the transitional arrangements at the transition date will need to have their benefits brought up to the level of members who were protected under those arrangements. The valuation of the IAS 19 liability should therefore take into account the expected impact.

27. As details of the remedy for the schemes are not yet available, there is uncertainty about the basis for valuing the impact of the judgements. Nonetheless estimation needs to be undertaken by actuaries based on the membership profile of the individual body, rather than the scheme as a whole. Therefore, bodies should be engaging actuaries to provide IAS 19 valuations using assumptions specific to each body, and the body's membership profile.

28. The appropriate accounting treatment in 2019/20 depends on whether the impact of the judgements was recognised in the pension liability in 2018/19 as summarised in the following table:

Recognised in IAS 19 liability in 2018/19	Treatment in 2019/20
Yes	Changes in the liability arising from changes in assumptions should be treated as an actuarial gain/loss
No	Recognition of the liability for the impact of the judgement as a past service cost

29. Bodies should consider the need to disclose information about the basis of estimation where these might have a significant risk of material adjustment to the carrying amount within the next 12 months.

Auditor action

Auditors should confirm that the impact of the judgements is properly reflected

Statutory other information developments

Good practice note on Management Commentaries

30. Professional Support has published a Good Practice Note following a review of the 2018/19 Management Commentaries within the annual accounts of Scotland's 32 councils. The review goes beyond basic compliance, and considers eight characteristics of financial reporting which Professional Support believes make for a high quality Management Commentary. The Good Practice Note is structured around these characteristics, and it discusses and highlights some of the good practice adopted by councils in relation to each one. The note also includes points for councils to consider in striving to achieve good practice.

31. The review was carried out by a team with knowledge of the relevant financial reporting framework. However, the team does not have a detailed understanding of each council's particular circumstances or the specific underlying transactions. The illustrations used in the Good Practice Note are all taken unchanged from councils' 2018/19 Management Commentaries.

32. Bodies are encouraged to use the findings in this Good Practice Note to assess and enhance their own Management Commentary.

Auditor action

Auditors should encourage bodies to use the Good Practice Note

Grant claims and other returns developments

Housing benefits

33. The Department for Work and Pensions (DWP) has issued the housing benefit subsidy claim form and notes for its completion for 2019/20 as well as:

- HB Circular A1/2020 and HB Circular A2/2020 to advise of respectively the benefits rates war pension rates from April 2020
- HB circular A3/2020 to set out changes to the severe disability premium process from March 2020.

Summary of auditor actions in this section

Paragraphs	Auditor actions
14	Pay due regard to TGN 2020/3(LG) when dealing with objections to the 2019/20 annual accounts
26 - 30	Confirm that the impact of the McCloud judgement is properly reflected in the IAS 19 liability at 31 March 2020
31 - 34	Encourage bodies to use the Good Practice Note on Management Commentaries

Contact point for this section

34. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk

Section 3

Central government sector

Auditing developments

Technical Guidance Note on risks of misstatement in 2019/20

35. Professional Support has published Technical Guidance Note (TGN) 2020/1 to provide auditors with guidance on planning and performing the audit of 2019/20 annual report accounts of central government bodies.

36. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement in 2019/20. The TGN supplements the Code of Audit Practice and auditors are expected to pay it due regard and use it as a primary reference source when performing 2019/20 audits.

Auditor action
Auditors should pay due regard to TGN 2020/1

37. The TGN structure comprises a number of modules:

- The Overview Module provides an overall introduction and covers risks of misstatement in areas that are pervasive to the financial statements as a whole.
- Modules 1 to 8 set out risks of misstatement for specific classes of transactions, balances and disclosures in the financial statements. These modules explain the appropriate related accounting treatment and set out the action auditors should undertake to evaluate whether the body has followed the required treatment.
- Module 9 covers irregularities in income and expenditure
- Module 10 covers the audited part of the Remuneration and Staff Report
- Module 11 sets out procedures for Statutory Other Information (i.e. Performance Report and Governance Statement).

38. The TGN also provides specific guidance on the application of the above modules to charitable NDPBs (Module 12) and, as explained in Section 3 of this bulletin, health boards (Module 13).

39. As part of the package of enhancements being made to the Technical Reference Library, a dedicated page* has been created for auditors to access which contains hyperlinks to each module. A version of the TGN which combines all the modules is also freely available from the Audit Scotland website.

2019/20 GBS account information

40. Professional Support intend obtaining information on account balances at 31 March 2020 for central government bodies from the Government Banking Service (GBS) and distribute them to relevant auditors.

Annual report and accounts developments

Revised 2019/20 FReM

41. HM Treasury has issued a revised version of the 2019/20 Government Financial Reporting Manual (the FReM).

42. There are no significant changes in requirements. Annex 5 has been added to this revised version to provide additional good practice guidance on narrative reporting.

2020/21 FReM

43. Treasury has issued the 2020/21 FReM. The main changes are in respect of the structure of the FReM which has been revised into four parts as set out in the following table:

Part	Chapters
A Principles, purposes and best practice of government financial reporting	2 on financial reporting principles and 3 on best practice in narrative reporting
B The form and content of Government annual reports and accounts	4 on the annual report and accounts, 5 on the Performance Report, 6 on the Accountability Report, and 7 on the financial statements
C Applying accounting standards to government annual reports and accounts	8 on adapting and interpreting standards
D Further guidance for government annual reports and accounts,	9 to 12 provides further guidance on specific areas and 13 on Whole of Government Accounts

44. Paragraph 2.4.1 introduces the concept that the four purposes of government financial reporting are to:

- maintain and ensure parliamentary control of government spending, enabling, in particular, Parliament to hold the Government accountable for its spending
- enable the public and researchers to understand and consider the value for money offered by public spending, so that they can make decisions about the effectiveness, efficiency, and economy of particular policies or programmes
- provide a credible and accurate record which can be relied upon
- provide managers with the information they require to run bodies efficiently and effectively.

45. Each of the four purposes relates to the needs of a different report user. Chapter 2 therefore discusses the importance of user engagement. It also clarifies that, for annual reports and accounts, the needs of Parliament as the primary user take precedence.

46. Chapter 3 is new and reflects lessons learned from the Government Financial Reporting Review which found a wide range of examples of good practice in narrative reporting. The new chapter provides guidance to help preparers improve reporting and refers to annexe 4 which contains links to resources for better narrative reporting.

47. Chapter 4 groups together all the high-level guidance relating to the annual report and accounts and provides an overview of the required format.

48. Chapter 5 on the Performance Report has been extensively revised and contains substantive changes to reporting requirements. The guidance on the performance analysis section is split into:

- mandatory requirements (paragraph 5.4.4)
- comply or explain requirements (paragraph 5.4.5)
- best practice recommendations (paragraph 5.4.6).

New Performance Report requirements

49. The new chapter 6 now covers revised requirements on the Accountability Report including a new requirement to disclose staff turnover in the Remuneration and Staff Report.

50. The remaining chapters 7 to 13 remain largely unchanged from the requirements in the previous sections of the FReM they are taken from.

Financial statements developments

Revised guidance on IFRS 16

51. Treasury has issued revised guidance on applying IFRS 16 on the central government sector. The guidance has been revised to reflect budgeting guidance and make minor clarifications.

2019/20 discount rates

52. Treasury has issued PES(2019)11* which announces the change in the discount rate for general provisions, post-employment benefits liabilities, and financial instruments as at 31 March 2020.

53. The nominal discount rates to be applied as at 31 March 2020 for discounting general provisions recognised under IAS 37 are set out in the following table:

Category	Period	Percentage
Short term	Within 5 years	0.51%
Medium term	Between 5 and 10 years	0.55%
Long term	Between 10 and 40 years	1.99%
Very long term	More than 40 years	1.99%

Auditor action
Auditors should refer to this guidance when auditing the 2019/20 financial statements

54. As nominal rates do not take inflation into account, cash flows require to be inflated separately. There is a rebuttable assumption that the inflation rates specified in the paper will be used (unless other rates are clearly more applicable). The specified rates are:

- 1.99% for up to two years from the year end
- 2% for after two years.

55. The discount rates for post employment benefits are set out in the following table:

Use	Rate from 31 March 2020
Real rate used for valuing unfunded pension scheme liabilities and early departure provisions	(0.5)%
Nominal rate for unwinding discount on liabilities (interest)	1.8%
Rate used for funded pension schemes	Based on returns from AA corporate bonds at 31 March

56. The financial instrument discount rates to be applied at 31 March 2020 are set out in the following table:

Type	Rate
Real rate when financial instrument indexed to RPI	0.7%
Nominal rate when financial instrument is not linked to an inflationary index	3.7%

57. The paper also specifies a rate to be used for leases under IFRS 16. The 2020 nominal lease discount rate of 1.27% is only relevant for transition to IFRS 16 and for new leases that commence or are remeasured between 1 January 2020 and 31 December 2020.

2019/20 disclosure guide

58. The National Audit Office (NAO) has issued the 2019/20 FReM Disclosure Guide which is designed to ensure that bodies covered by the FReM have prepared their 2019/20 financial statements in the appropriate form and have complied with all disclosure requirements.

59. The guide is cross-referenced to the 2019/20 FReM, individual financial reporting standards, and the Companies Act 2006. Auditors will need to generate a tailored checklist by selecting the criteria that are material to their audited body.

Auditor action
Auditors should consider requesting that bodies complete this guide

60. While the guide is designed primarily for the NAO's internal use, auditors in Scotland may also find it helpful. When checking that the FReM's disclosure requirements have been met, auditors should:

- consider requesting that the body completes the NAO's 2019/20 disclosure guide for the financial statements
- investigate the reasons for any non-compliance that the guide highlights
- evaluate whether the body's responses in the guide are consistent with auditor's knowledge.

Remuneration and staff report

Guidance on 2019/20 disclosures

61. The Cabinet Office has issued EPN 597 2019/20 Disclosure of salary, pension and compensation information to provide guidance on the preparation of the pay pension and compensation disclosures in the remuneration and staff report for 2019/20. Example disclosures are provided at Annex 13C.

62. There are no significant changes to the remuneration disclosures set out from 2018/19.

63. The guidance does not reflect the application of the FReM's requirements to Scottish bodies and therefore auditors should refer to Module 11*of Technical Guidance Note 2020/1.

Auditor action
Auditors should refer to this guidance when auditing the Remuneration and Staff Report in the 2019/20 annual report and accounts

Statutory other information developments

Revised internal control checklist

64. The Scottish Government has issued Finance Guidance Note 2020/1 which announces amendments to the certificates of assurance section of the Scottish Public Finance Manual.

65. The internal control checklist has been updated, with new questions added on:

- assessing the level of skills and training of those staff directly managing key risks
- the arrangements in place for the realisation of benefits and capturing lessons from major investment projects
- assurance on grant awards and grant manager skills and training
- ensuring appropriate contracts are place for all procurement.

Wider audit scope developments

Financial management

66. The Scottish Government has issued Finance Guidance Note 2020/3 to announce recent additional guidance for Accountable Officers during the current Covid-19 situation. Some key aspects of the guidance are as follows:

- Director Generals are asked to consider which activities may be reduced, stopped, or re-profiled, thereby releasing savings that can be redirected to cover the cost of COVID-19
- Where actions are required to be taken as a priority in order to support the health and safety of the public, Accountable Officers should document this decision and seek subsequent approval.
- Director Generals should manage any COVID-19 spend of £1 million or less but should keep track of it. Where expenditure exceeds that amount, a template at Annex A should be submitted for sign off by the Cabinet Secretary.
- Accountable officers should also assess whether any expenditure undertaken as a result of the outbreak has appropriate statutory power. If there is no statutory power, it may still be possible to undertake the expenditure if Ministers possess the necessary common law powers or the expenditure is not of a continuing nature.

67. The Scottish Government has also issued Finance Guidance Note 2020/4 to advise of a relaxation of normal controls to allow expiring leases to be extended for up to one year in lieu of submitting formal business cases.

Summary of auditor actions in this section

Paragraphs	Auditor actions
35 - 39	Pay due regard to TGN 2020/1 when auditing the 2019/20 annual report and accounts
52 - 57	Refer to the guidance on 2019/20 discount rates
58 - 60	Consider requesting bodies to complete the 2019/20 disclosure guide
61 - 63	Refer to the guidance on remuneration disclosures when auditing the 2019/20 Remuneration and Staff Report

Contact point for this section

68. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 4

Health sector

Auditing developments

Technical guidance note on risks of misstatement in 2019/20

69. Professional Support has published Module 13 of TGN 2020/1 to provide:

- guidance on applying the other modules to the audit of the annual report and accounts of health boards
- supplementary guidance on the risks of misstatements in the areas specific to health boards.

Auditor action
Auditors should use this guidance when performing the audit of the 2019/20 annual report and accounts

2019/20 model independent auditor's reports

70. Professional Support has published Technical Guidance Note 2020/2(H) 2019/20 Independent Auditor's Report for Health Boards to provide auditors with the model Independent Auditor's Reports which should be used for the 2019/20 annual report and accounts. The technical guidance note also provides application guidance on their use.

71. In the interests of consistency, auditors are required to use the relevant model report in appendices 1 to 2 of the Technical Guidance Note as a condition of their audit appointment. The only exception to using the wording in each model is to tailor the terminology to reflect local circumstances.

72. There have been no significant changes to the model Independent Auditor's Reports for 2019/20, although some enhancements have been made to the guidance to make the required auditor actions clearer.

Auditor action
Auditors should use this TGN when reporting the audit of the 2019/20 annual report and accounts and complete the relevant checklists

Review of central work on CNORIS

73. Professional Support will be undertaking a review of the work carried out by the NHS Central Legal Office (CLO) relating to the Clinical Negligence and Other Risks Indemnity Scheme (CNORIS). The objective of the review is to establish the extent to which the information prepared using the work of the CLO, as a management expert under ISA (UK) 500, can be used as audit evidence.

74. Professional Support will also evaluate the appropriateness of the methodology adopted by the Scottish Government to establish the total national liability for CNORIS. The review will focus on the estimation of the liability as at 31 March 2020 with a view to assessing the reliability of the methodology used for 2019/20.

75. Professional Support will then provide auditors with the outcome of the reviews to:

- inform auditors' evaluation of the relevance and reliability of the information prepared by the CLO as audit evidence
- provide assurance on the methodology used in the preparation of the CNORIS figures as at 31 March 2020 which are provided to boards.

Annual report and accounts overall developments

2019/20 accounts manual

76. The Scottish Government has issued the 2019/20 Manual for the Annual Report and Accounts of NHS Boards* (accounts manual) to complement the guidance contained in the 2019/20 FReM.

Auditor action
Auditors should refer to the accounts manual when auditing the 2019/20 annual report and accounts

77. The main changes included in the accounts manual compared with 2018/19 are summarised the following table:

Area	Change
Performance Report	The disclosure on financial performance on page 8 has been amended to reflect the introduction of the three year planning cycle which provides flexibility to incur a 1% overspend within an overall breakeven period of 3 years.
Remuneration and Staff Report	The guidance on disclosure of information in the remuneration report has been amended to be consistent with the FReM and General Data Protection Regulations. Boards are required to advise individuals in advance on the intention to disclose. Previously the manual required boards to obtain consent for disclosure. Page 31 has been amended to deduct staff costs charged to capital expenditure in the reconciliation to income and expenditure
Performance Report and Accountability Report generally	These sections have been amended to clarify which disclosures are required by the FReM or the Scottish Government which are suggested guidance to assist boards.
Summary of resource outturn (SoRO)	The SoRO has been moved from the foot of the Statement of Comprehensive Net Expenditure to note 2. This is to help clarify that the SoRO is not a primary financial statement.
Pension costs	The narrative at Note 19 has been updated for pension scheme disclosure requirements and qualifying earnings.

Financial statements developments

2019/20 capital accounting manual

78. The Scottish Government has issued the 2019/20 NHS Capital Accounting Manual* (CAM) to interpret the accounting guidance contained in the 2019/20 FReM on capital accounting issues in the health sector.

79. There are no significant changes from the 2018/19 CAM.

Auditor action
Auditors should refer to the CAM when auditing property, plant and equipment in 2019/20

Guidance on income from R&D contracts

80. The NHS Scotland Technical Accounting Group has issued guidance on applying IFRS 15 to research and development contracts.

81. The guidance covers three aspects of the contracts as summarised in the following table:

Aspect	Summary of guidance
Accounting for staged payments	As the board as an enforceable right to payment for performance completed to date, the performance obligation is regarded as satisfied over time. Income and expenditure should be recognised and presented gross as the contract progresses.
Treatment of surplus on commercial contracts	A liability should be recognised at the year end for the element of any surplus due to partners.
Recovering costs on infrastructure support and capacity building	An asset should be recognised where such costs are expected to be recovered.

Wider audit scope developments

Revised financial planning arrangements

82. The Scottish Government has issued a letter* on revised financial planning arrangements over the coming months. The Scottish Government has reviewed boards' draft mobilisation plans, and has issued a template to identify a financial baseline for additional costs in relation to Covid-19. Boards have been advised to provide as much information as possible about the assumptions used, particularly in terms of redeployment of staff and other resources from non-urgent elective care.

83. Boards are not required to submit financial reporting performance returns for months 11 and 12. Resource and capital outturns for 2019/20 are assumed to be in line with the position already agreed with boards. Final funding letters will be issued with the necessary authorisation for 2019/20 outturn.

Contact point for this section

84. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 5
Professional matters

Auditing developments

Revised auditing standards

85. The Financial Reporting Council (FRC) has issued a number of revised auditing standards that apply to financial periods commencing on or after 15 December 2019. The main changes are summarised in the following table:

ISA (UK)	Summary of change
250A Consideration of Laws and Regulations in an Audit of the Financial Statements	Paragraph 13-1 has been added to require an auditor, when performing risk assessment procedures under ISA (UK) 315, to consider whether there are any indications of non-compliance with laws and regulations. Application guidance has been added at paragraph A11-3 on considering both quantitative and qualitative factors, including in circumstances where the direct effect on the determination of amounts and disclosures in the financial statements is not quantitively material. For example, acts of non-compliance may not generate material fines or penalties, but may have a direct effect on disclosures due to the nature of the entity where such disclosure is important to users of the financial statements.
700 Forming an Opinion and Reporting on the Financial Statements	Paragraph 29-1 has been revised so that the application of the requirement to explain in the report the extent to which the audit was considered capable of detecting irregularities has been extended from Public Interest Entities to all bodies. Application guidance has been added at paragraphs A39-1 to A39-3. The FRC has issued a revised bulletin to provide illustrative auditor's reports for the private sector.
701 Communication Key Audit Matters in the Independent Auditor's Report	Paragraph 13(b) has been revised to require auditors to report significant judgments made by the audit team with respect to each matter. The revisions to paragraph 16-1 are requirements to: • specify the threshold for performance materiality, in addition to materiality • provide an explanation of the significant judgments made by the auditor in determining materiality and performance materiality.
720 The Auditor's Responsibilities Relating to Other Information	Paragraph 22-1 has been added to require an auditor, if required to report on statutory other information, to include in the auditor's report a: • description of the auditor's responsibilities relating to the statutory other information. Paragraph A53-2 advises that this may be in the body of the report, an appendix or by a reference to a website • conclusion thereon. Application guidance has been added on judging the materiality of misstatements

Proposed changes to standard on auditing estimates

86. The FRC has issued an exposure draft of proposed revisions to ISA (UK) 315. The proposed changes reflect recent revisions to the international standard, and are summarised in the following table:

Area	Proposal
IT business environment	This includes requiring the auditor to understand the entity's use of IT in its business, the related risks and the system of internal control addressing such risks.
Automated audit tools and techniques	Additional application guidance on the use of automated tools and techniques by auditors.
Enhancing professional scepticism	An emphasis has been added on the need for auditors to not bias their work toward obtaining corroborative evidence or excluding evidence that is contradictory. A new requirement for the auditor, towards the end of the risk assessment process, to consider all audit evidence obtained from performing risk assessment procedures, whether corroborative or contradictory.
Purpose of risk assessment	Clarification has been added that the purpose of performing risk assessment procedures is to obtain audit evidence that provides an appropriate basis for the identification and assessment of the risks of material misstatement and the design of further audit procedures
Inherent risk factors	The concept of 'inherent risk factors' has been introduced to assist the auditor in identifying events or conditions that may affect the susceptibility of assertions about classes of transactions, account balances or disclosures to misstatement.
Significant class of transactions, account balances or disclosures	This new concept refers to those classes for which there are assertions with an identified risk of material misstatement (referred to as relevant assertions).
Spectrum of inherent risk	This new concept applies to the extent to which inherent risk varies
Significant risk	This relates to an identified risk of material misstatement for which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur.
Control risk	Guidance has been added explaining that, if the auditor does not plan to test the operating effectiveness of controls, control risk should be assessed as the same as the assessment of inherent risk.

87. The effective date of the revised standard is proposed to be accounting periods beginning after 15 December 2021. Comments should be sent to AAT@frc.org.uk by 3 April 2020.

Report from the Brydon Review

88. The Bryden Review has issued a report which recommends to the UK Government improvements in the quality and effectiveness of the audit of Public Interest Entities. A selection of some of the recommendations that could have relevance to the public sector are set out in the following tables.

Redefinition of audit and its purpose

Subject	Paragraph	Recommendation
Purpose	5.1.3 – 5.1.4	The following statement should be adopted by the Audit, Reporting and Governance Authority (ARGA), and the UK Government should enshrine it in the Companies Act: “The purpose of an audit is to help establish and maintain deserved confidence in a company, in its directors and in the information for which they have responsibility to report, including the financial statements.”
New information	5.3.2	Auditors should be free to include original information, materially useful to a wide range of users, in their audit report, and not be confined to commenting on information stated by directors.
	5.3.12	The obligation to read and consider other information in the Annual Report be extended to material outside the Annual Report.
New profession	6.0.11	ARGA acts to create a new profession of corporate auditing, establishing the necessary professional body, to encompass today’s auditors and others with appropriate education and authorisation. ARGA would be the statutory supervisory body for that profession.
	6.0.16	There should be one encompassing descriptor with a new definition - "corporate auditor" (including environmental auditors, cyber security auditors and financial statement auditors).
Establishing the role of Principles	6.3.4	The Principles of Corporate Auditing (set out at paragraph 6.4.2) should be established to form an overarching framework governing the behaviour of corporate auditors, and standards and rules should sit within this framework.
Principles of Corporate Reporting	6.4.5	Each audit report should contain a statement to the effect that in conducting the audit the auditor has acted faithfully in accordance with the Principles of Corporate Auditing.
Audit fees	9.4.5	The audit fees should be shown on the face of the profit and loss account.
	9.4.9	The audit committee chair should be delegated to negotiate the fees for the relevant audit work. The Board should agree an ‘assurance budget’ for the audit committee which would include the fees.
	9.4.14	Audit firms should establish an independent fee-setting function making its decisions separately from those conducting the audit.

True and fair

Subject	Paragraph	Recommendation
Presents fairly	11.9	The Companies Act and ISA (UK) 700 should be amended to replace “true and fair” with “present fairly, in all material respects”.
Override	11.15	Auditors should judge any use of an ‘override’ in the context of their obligation to be faithful to the Principles of Corporate Auditing.

Accounting records

Subject	Paragraph	Recommendation
Adequate accounting records	12.4	The Companies Act should clarify what is meant by "adequate accounting records". There should be an obligation for auditors to assess whether the directors have maintained accounting records to a standard beyond the minimum level necessary for an audit to be performed.

Fraud

Subject	Paragraph	Recommendation
Clarity of auditor obligations	14.1.5	ISA (UK) 240 should be amended to make clear that it is the obligation of an auditor to endeavour to detect material fraud in all reasonable ways.
Directors' obligations	14.2.2	Directors should report on the actions they have taken to fulfil their obligations to prevent and detect material fraud against the background of their fraud risk assessment.
Forensic skills	14.3.5	The auditor's report should state explicitly the work performed to conclude whether the directors' statement regarding the actions they have taken to prevent and detect material fraud is appropriate. Auditors should also state what steps they have taken to assess the effectiveness of the relevant controls and to detect any such fraud.

Signalling concern

Subject	Paragraph	Recommendation
Eternal signals	16.4	There should be an obligation on the auditors to report to both the audit committee and the shareholders on the extent to which their work has been influenced and informed (or not) by any external signals which might imply enhanced risk in the company.
Menu of signals	16.7	ARGA should develop a menu of possible signals [examples set out at paragraph 16.8] and the auditors should report against the relevant parts of that menu.

Communicating judgements

Subject	Paragraph	Recommendation
Differences of view	17.0.4	The audit committee should describe any debate regarding differences of view between management and auditors and its outcome, including the justification for the agreed treatment. For example, where the differences of view would have led to material changes in valuation, even when these differences have been resolved, the audit committee should report on the range of the initial views and where in that range the agreed valuation lies.
Culture	17.2.6	ARGA should develop a series of examples which would illustrate the types of culture that auditors should reference in their report where there is an observed disconnect between the culture of the company claimed by the directors and the behaviour observed by the auditors.
Quality of estimates	17.4.6	The auditor's report should include some substantive discussion of the key areas of measurement uncertainty and provide information on the ranges and sensitivities associated with the point estimates for those measurements.

Alternative Performance Measures and Key Performance Indicators

Subject	Paragraph	Recommendation
Alternative Performance Measures	20.1.5	Alternative Performance Measures (i.e. figures based on International Financial Reporting Standards [IFRS] adjusted by management to make the underlying performance of the company more visible) should be subject to audit.
Key Performance Indicators	20.2.8	Any Key Performance Indicators used for the purpose of calculating executive remuneration should be subject to audit.

Technology

Subject	Paragraph	Recommendation
Obstacles to progress	24.1.8	ARGA should work with auditors to create the necessary protections and policies for audit to be able to use data from the companies they audit in order to promote better quality audits.
	24.1.11	Auditors should explain in the audit report the reasons for the necessity and basis of any sampling techniques used in conducting the audit.

Auditor liability and transparency

Subject	Paragraph	Recommendation
Greater transparency	25.2.5	Individual statutory audit reports detail the number of hours spent in conducting the audit by grade of auditor.

Accounting developments

Proposed changes in presentation and disclosure requirements

89. The International Accounting Standards Board has issued an exposure draft of proposals on improving how information is communicated in the financial statements.

90. The central proposal is to replace IAS 1 Presentation of Financial Statements with a new standard containing new requirements on presentation and disclosures in the financial statements.

91. Responses require to be sent to commentletters@ifrs.org by 30 June 2020.

It is proposed to replace IAS 1 with new presentation and disclosure requirements [

Structure of the statement of profit or loss

92. The exposure draft proposes that an entity present the following new subtotals in the statement of profit or loss:

- operating profit or loss
- operating profit or loss and income and expenses from integral associates and joint ventures
- profit or loss before financing and income tax.

93. In applying these proposed new subtotals, an entity would present in the statement of profit or loss income and expenses classified in the following categories:

Categories	Types of income and expenses
Operating	Those from an entity's main business activities. This may include from investments and financing activities if they are a main business activity.

Categories	Types of income and expenses
Integral associates and joint ventures	Those from associates and joint ventures that are integral to the main business activities of an entity and hence do not generate a return individually and largely independently of the other assets of the entity.
Investing	Those from assets that generate a return individually and largely independently of other resources held by the entity
Financing	Those from cash and cash equivalents, liabilities arising from financing activities; and the unwinding of discounts on pension liabilities and provisions.

Aggregation and disaggregation

94. Paragraphs 25 to 28 of the exposure draft propose principles and general requirements on the aggregation and disaggregation of information, applicable both to presentation in the primary financial statements and disclosures in the notes. This includes requirements that

- items should be classified and aggregated on the basis of shared characteristics
- aggregation and disaggregation in the financial statements should not obscure relevant information or reduce the understandability of the information presented or disclosed.

95. When presenting information in the primary financial statements or disclosing information in the notes, the description of the items should faithfully represent the characteristics of those items. Using a label such as ‘other’ to describe a group of such items would not faithfully represent those items without additional information.

Unusual income and expenses

96. There is a proposal to introduce a definition of ‘unusual income and expenses’, and to require all entities to disclose unusual income and expenses in a single note.

97. This is defined at paragraph 100 of the exposure draft as income and expenses with limited predictive value. This would be the case where it is reasonable to expect that income or expenses of a similar type will not arise for several years.

Management performance measures

98. There are proposals to introduce a definition of ‘management performance measures’ and require an entity to disclose them in a single note. Management performance measures are subtotals of income and expenses that:

- are used in public communications outside financial statements
- complement totals or subtotals specified by IFRS
- communicate to users of financial statements management’s view of an aspect of an entity’s financial performance.

99. An entity would comply with the general requirements in IFRS when it provides these measures, e.g. each performance measure must faithfully represent an aspect of the financial performance of the entity. The exposure draft also proposes to specify the information an entity would be required to disclose about management performance measures, including a reconciliation to the most directly comparable total or subtotal specified by IFRS.

Contact point for this section

100. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Technical Bulletin 2020/1

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or **info@audit-scotland.gov.uk**

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Technical Bulletin 2020/2

Technical developments and emerging risks from April to June 2020

Prepared for appointed auditors and audited bodies in all sectors

25 June 2020

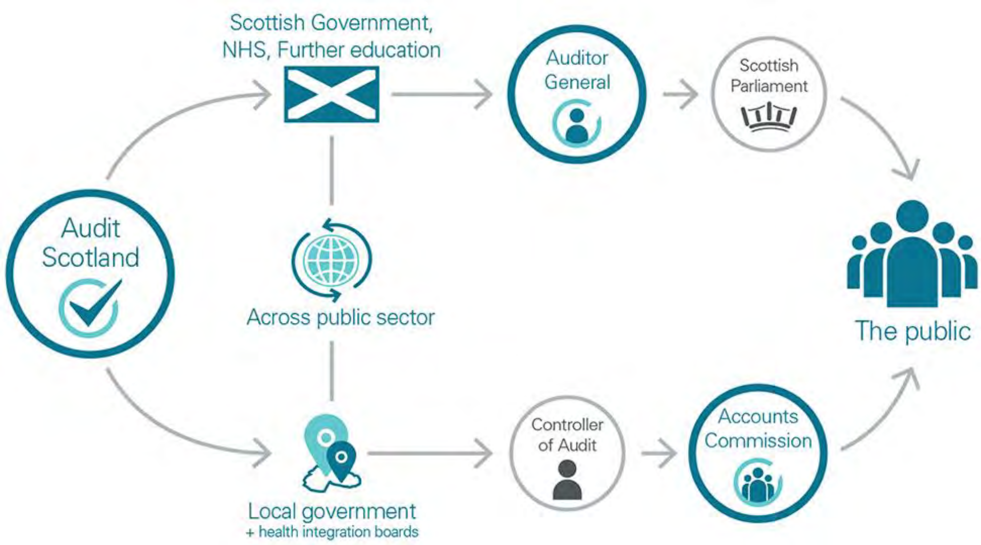
Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.

- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.

- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money

- reporting our findings and conclusions in public

- identifying risks, making clear and relevant recommendations.

Contents

Introduction

Purpose

1. The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector and on professional matters during the quarter
- guidance on any emerging risks identified in the quarter.

Technical Bulletins provide information on developments and guidance on emerging risks

2. Appointed auditors are required to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require to be aware of. It may still be necessary for auditors to read the source material if greater detail is required. These can be accessed by using the hyperlinks. They are also available from the Technical Reference Library* maintained by Professional Support.

3. The actions by auditors recommended by Professional Support in respect of each item are highlighted in red and are also summarised at the end of each section.

4. Technical Bulletins are also published on the Audit Scotland website and therefore are available to audited bodies and other stakeholders. Hyperlinks indicated with an asterisk link to the Technical Reference Library and therefore are active only for auditors.

Highlights summary

5. Particular attention is drawn in the following table to certain items in this Technical Bulletin:

Professional Support has published an addendum to the guidance on planning 2019/20 audits [see paragraph 7]	The Public Audit Forum has issued an exposure draft of proposed changes to PN 10 [see paragraph 9]	Professional Support has provided technical advice to auditors on a number of issues [see paragraphs 14, 48, 64, and 82]
The Scottish Government has issued guidance on the application of the Coronavirus (Scotland) Act 2020 to local government annual accounts [see paragraph 15]	Professional Support has published model 2019/20 Independent Auditor's Reports for local government [see paragraph 23] and central government [see paragraph 65]	CIPFA has issued guidance on the 2019/20 financial statements of local government bodies [see paragraph 31]
PWC has issued a report on IAS 19 figures at 31 March 2020 [see paragraph 38]	The Scottish Government has issued circulars on a grant funding scheme to assist eligible businesses during the COVID-19 crisis [see paragraph 44]	The Scottish Government has issued revised statutory guidance on the Management Commentary [see paragraph 49]
HM Treasury has issued an addendum to the 2019/20 FReM [see paragraph 60]	TAG has issued additional guidance on the 2019/20 annual report and accounts of health boards [see paragraph 73]	Professional Support has issued a report on CNORIS [see paragraph 81]

Contact point

6. The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – pobrien@audit-scotland.gov.uk.

Feedback on this Technical Bulletin is welcome

Section 1

Cross sector

Addendum to guidance on planning 2019/20 audits

7. Professional Support has issued an addendum to the guidance for auditors on planning their 2019/20 audits. The addendum varies specified elements of the original guidance published in October 2019 which have had to be revised as a result of the impact of the COVID-19 suppression measures on the delivery of audits. These include:

- providing guidance on identifying further significant risks as a result of the impact of COVID-19
- explaining the impact on the timetable for producing the annual accounts and consequent amendments to the submission deadlines
- confirming the acceptability of electronic signatures in the annual accounts.

8. The addendum, like the original guidance, supplements the Code of Audit Practice, and auditors are therefore required to pay due regard to it when planning their 2019/20 audits.

Auditor action
Auditors should pay due regard to the addendum to 2019/20 planning guidance

Proposed changes to practice note 10

9. The Public Audit Forum has issued an exposure draft of proposed changes to Practice Note 10 Audit of Financial Statements and Regularity of Public Sector Bodies in the UK (PN 10).

10. PN 10 sets out how auditors of public sector bodies in the UK apply auditing standards to their work on financial statements, with the aim of supporting consistency in their application. It also provides guidance on the approach to the audit of regularity.

11. A summary of the proposed changes to PN 10 is provided in the annex to the Invitation to Comment. Some key proposed changes are summarised in the following table:

Proposed changes to PN 10

ISA (UK)	Key proposed changes
540	The issue in December 2019 of the revised standard on auditing estimates has been reflected in the revised draft. Guidance has been added at paragraph 1-116 on inherent risk factors relevant to the public sector, with examples such as: • a very high degree of estimation uncertainty caused by the need to project forecasts far into the future • the lack of available comparators for estimates that are unique to the public sector, such as the valuation of important public assets the existence of possible constructive obligations created by political statements or past practice of carrying out actions that may be expected of public authorities.
560	The guidance on determining the date the financial statements are authorised for issue and the date they are issued has been refreshed. Paragraph 1-136 has been amended to advise that central government financial statements are considered to be issued on the date of laying rather than the date of despatch for laying.
570	The revised standard on going concern has been reflected. In addition, paragraphs 1-148 to 1-183 have been extensively reordered to clarify what auditors should do when the financial reporting framework requires a going concern basis of accounting due to the continued provision of services.

ISA (UK)	Key proposed changes
720	Paragraph 1-124 has been added to provide guidance on when the reporting framework requires that the 'other information' presented is fair, balanced and understandable. Paragraph 1-126 has been added on statutory other information, on which the auditor is required to express a positive statement in the auditor's report.

12. Comments on the exposure draft should be sent to PracticeNote10@public-audit-forum.org.uk by 31 August 2020.

Deferral of IFRS 16 Leases

13. The Financial Reporting Advisory Board (FRAB) and the CIPFA/LASAAC Local Authority Code Board have decided to defer the effective date of IFRS 16 Leases in the public sector until 1 April 2021. This is to recognise that bodies' preparations are being adversely affected by dealing with the COVID-19 crisis.

Advice to auditors

14. The following table summarises a request for technical advice recently made by auditors to Professional Support in respect of the audit of the 2019/20 annual accounts which applies to all public bodies, along with the advice offered:

Auditor Action
Auditors should consider the application of this advice to their own audits

Property, plant and equipment

How should auditors respond where a professional valuer has declared a 'material uncertainty' in their valuation report on a property?
RICS guidance is clear that the declaration of a material uncertainty in a valuer's report does not mean that the valuation cannot be relied upon or that there is a misstatement. However, it indicates that less certainty can be attached to the valuation than would otherwise be the case. It is important that audited bodies disclose in the notes to the financial statements an adequate explanation of the estimation uncertainty in accordance with paragraphs 125 of IAS 1 Presentation of Financial Statements. The disclosure should help users understand the judgements that the body has made. Auditors should evaluate whether the disclosures adequately explain the uncertainty and the impact on the amounts recognised in the financial statements. Auditors should consider whether it is appropriate to include an Emphasis of Matter paragraph under ISA (UK) 706 in the Independent Auditor's Report. This would be the case where: • the matter is appropriately presented and disclosed in the financial statements • a modified opinion is not required • the matter is considered to be of such importance that it is fundamental to users' understanding of the financial statements.

Should a car park be treated separately from the land it is on for depreciation purposes?
IAS 16 Property, Plant and Equipment requires buildings to be accounted for separately from the underlying land. Land with an unlimited useful life is not depreciated. Buildings have a finite useful life and are depreciated. In the case of a car park, the appropriate classification may depend on its nature. For example, a multi-story car park is clearly a building whereas it may be acceptable to classify an area of spare land with no road surface as land. An important indicator is whether a valuer has attributed a useful life to the car park. Where a useful life has been attributed to the car park, it should be separated from the land and depreciation should be charged over that life.

Grants and other income

When should a donation for the construction of an asset be recognised?

The recognition of a donation as income can be deferred if there is a condition which requires the donation to be returned if an asset is not constructed. Recognition depends on the wording of the condition attached to the donation and the progress with construction. For example:

- Where construction takes place in the year of receipt, the donation should be recognised as income immediately.
- Where construction does not take place in the year of receipt, but there is reasonable assurance that the asset will be constructed, the donation may be recognised as a deferred credit.
- Where construction starts but is not completed by the year end, subject to the wording of the condition, Professional Support's view is that it may still be appropriate to recognise the donation as income in that year provided the body can demonstrate a clear intention to complete the asset.
- Where it becomes the case that construction will not be completed, and hence it is expected that the condition will be breached, the deferred credit or income should be derecognised and the obligation to return the donation recognised as a liability.

Summary of auditor actions in this section

Paragraphs	Auditor actions
1 - 2	Pay due regard to the addendum to 2019/20 planning guidance
8	Consider the application of the advice from Professional Support to their own audits

Section 2
Local government sector

Annual accounts overall developments

Coronavirus (Scotland) Act 2020

Bodies can decide not to comply with statutory duties

15. Schedule 6 of the Coronavirus (Scotland) Act 2020 amends certain statutory duties of public bodies in light of the impact of COVID-19 suppression measures. The Scottish Government has issued guidance in Finance Circular 10/2020 on the application of the powers contained in the Act to local government.

16. Part 3 of schedule 6 covers statutory duties that require a public body to publish a report in connection with the exercise of its functions. The body may decide to postpone complying with the duty if compliance would be likely to impede its ability to take effective actions against coronavirus. If so, the body must:

- publish a statement to that effect by the date by which the report is due (or as soon as reasonably practicable thereafter); and
- comply with the duty as soon as reasonably practicable.

Each body can determine a revised accounts timetable

17. The finance circular advises that the provisions in part 3 allow each local government body to determine its own revised timetable for the production and publication of its annual accounts. This means that the requirements in The Local Authority (Scotland) Regulations 2014 to:

- publish the unaudited accounts by 30 June can be postponed. The guidance recommends that the statement advising of the postponement be published by 17 June as that would normally be the latest date for advertising the unaudited accounts. It sets out the points to be covered in the statement on page 5
- meet to consider the unaudited accounts by 31 August can be postponed to within 2 months of publication
- publish the audited annual accounts by 31 October can be postponed. The Scottish Ministers consider it reasonable that publication should be by 30 November. The statement advising of the postponement requires to be published before 30 September (as that is the date the Act expires). The statement should also set out when the body will meet to consider the audited accounts.

18. Part 3 also applies to statutory duties that require a public body to give notice of where a document may be inspected, or make available a document for inspection in a particular manner. A body may decide not to comply with the duty if it is of the view that doing so may give rise to a significant risk of the transmission of coronavirus.

19. Where a body decides not to comply, it must publish or make available the document in an electronic format, or if that is not possible a statement to that effect. When the body considers that there is no longer a significant risk of transmission of coronavirus, it must ether:

- take such steps to comply, or
- publish a statement indicating that it is not complying and setting out the reasons for not doing so.

20. The finance circular advises that where it is not possible to allow an interested person access to council offices to inspect the unaudited accounts and related documents, the body can decide under the Act not to comply with the statutory requirements in respect of inspection. However, the guidance suggests that:

- publication of the request, together with the documents provided electronically, should be made in the same place on the website as the inspection notice

- when it is not possible to provide the information in electronic format the request, together with the statement that the body will not comply, should also be published in the same place on the website as the inspection notice. The notice should explain the process where it is not possible to provide that information electronically (i.e. body to contact them to provide access when there is no longer a significant risk of the transmission of coronavirus).

21. As a result of the amended requirements for the inspection of the unaudited accounts, Professional Support has published a revised version of Technical Guidance Note 2020/3(LG).

22. Other matters covered by the guidance in the finance circular include:

- Where a local authority has experienced difficulties in getting the assurances required, for example annual assurance certificates or similar, this should be explained.
- Section 95 officers will need to consider their own circumstances when determining whether they need to qualify their statement regarding whether the financial statements give a true and fair view.
- The Scottish Government has no objection to the use of electronic signatures, but it is for each body to ensure the security of those signatures.

Auditing developments

2019/20 model independent auditor's reports

23. Professional Support has published Technical Guidance Note 2020/5(LG) 2019/20 Independent Auditor's Report for Local Government Bodies to provide auditors with the model Independent Auditor's Reports which should be used for the 2019/20 annual accounts.

24. Section 101(4) of the Local Government (Scotland) Act 1973 requires auditors to place a certificate on a local government body's annual accounts and for that certificate to be in the form prescribed by the Accounts Commission. Auditors are required by the Code of Audit Practice to prepare their Independent Auditor's Reports (i.e. the certificate) in accordance with the TGN.

25. The model Independent Auditor's Reports set out in Appendices 1 to 5 of the TGN have been tailored to reflect local government legislation and augmented by the reporting requirements of the Accounts Commission. There have been no significant changes to the model Independent Auditor's Reports for 2019/20.

26. The TGN also provides guidance on the amendments that require to, or may, be made to the wording in the models in the form of auditor actions. Some enhancements have been made to the guidance to make the required auditor actions clearer and to clarify the use of electronic signatures. Auditors should complete for each report the checklist at Appendix 6 which provides a list of those auditor actions.

27. Any proposed modifications to any audit opinion or conclusion, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with Professional Support in advance of finalising the report.

28. Auditors should use this TGN when reporting on 2019/20 audits.

Auditor action
Auditors should use this TGN when reporting the audit of the 2019/20 annual accounts and complete the checklist

Financial statements developments

Application of 2019/20 accounting code

29. Technical Bulletin 2020/1 drew attention (at paragraph 17) to proposals to replace the 2019/20 Code of Practice on Local Authority Accounting in the UK (accounting code) with a simplified version that was being prepared.

30. The CIPFA/LASAAC Local Authority Code Board (CIPFA/LASAAC) subsequently issued a statement advising that it had decided not to implement the simplification proposals. The requirements of the 2019/20 accounting code continue to apply in full.

The 2019/20 accounting code continues to apply in full

Guidance on closing 2019/20 financial statements

31. The Chartered Institute of Public Finance And Accountancy (CIPFA) has issued Bulletin 5 Closure of the 2019/20 Financial Statements which provides guidance on the following areas of the 2019/20 financial statements that are relevant to Scottish bodies:

- Deferral of the implementation of IFRS 16 Leases
- Going concern accounting basis
- Accounting for COVID-19 support measures
- Financial reporting issues arising from COVID-19.

Deferral of the implementation of IFRS 16

32. Paragraphs 37 to 39 of the bulletin confirm that the implementation of IFRS 16 Leases has been deferred until 2021/22. Appendix 2 outlines the key changes proposed following the consultation on the adoption of IFRS 16 by local government and provides updates on the early implementation guidance.

Implementation of IFRS 16 has been delayed a year

Going concern accounting basis

33. Paragraphs 43 to 45 highlight that the accounting code's requirement to use the going concern basis of accounting mean that local government bodies cannot apply paragraph 25 of IAS 1 in respect of making an assessment of the body's ability to continue as a going concern.

34. This requirement applies regardless of the impact of COVID-19 on local government financial sustainability because the rationale for requiring the going concern basis remains unchanged.

35. However, local government bodies nevertheless need to report on the impact of the COVID-19 in, for example, the relevant liquidity reporting requirements under IFRS7 Financial Instruments: Disclosures and credit risk disclosures.

Going concern basis of accounting remains appropriate but financial sustainability issues to be reported

Accounting for COVID-19 support measures

36. Paragraph 55 advises that councils should consider whether they are acting as principal or agent in respect of the COVID-19 grant schemes (see paragraph 44 of this Technical Bulletin) and account for the grant accordingly. Paragraph 53 advises that, in the case of similar schemes operating in England, a council is not acting on its own behalf.

Financial reporting issues arising from COVID-19

37. The bulletin (paragraphs 63 to 97) provides guidance on a number of financial reporting issues arising from COVID-19. Some key points are summarised in the following table:

Area	Summary of guidance
Events after the reporting period	Bodies need to continually review and update their assessment of events up to the date the financial statements are authorised for issue. Examples of non-adjusting events might include after the year end: the closure of local offices; abnormally large changes in asset values; and major changes in service delivery. Examples of adjusting events include: the valuer able to access better information on asset values as at the year end; the receipt of information indicating that an asset was impaired; and notification of changes to grant entitlements.
Property, plant and equipment	The body's property (e.g. offices) may be impaired because it was not in use at 31 March. Where valuers include a 'material valuation uncertainty' declaration in their reports, bodies should consider the significance. However, this may not mean that valuers are unable to provide a reliable valuation for the asset. Bodies should be clear in their instructions to the valuer what estimation uncertainty means in financial reporting terms. The accounting code requires the disclosure of information about the assumptions concerning the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities, within the next financial year.

Area	Summary of guidance
Financial instruments – fair value valuation	Fair value measurements for financial instruments, including investment properties, require to take into account the conditions at 31 March. IFRS 13 (paragraphs B37 to B42) provides special arrangements for circumstances where the volume of activity for an asset (or a liability) has significantly decreased. Transactions may be adjusted where they are not orderly (see paragraphs B43 to B44). Where fair value measurements had been based on market valuations and observable inputs, and these are either no longer available or reliable, IFRS 13 (paragraphs 72 to 90 and paragraphs B5 to B11) allows for changes in the inputs used and for different valuation techniques to be used.
Financial instruments – expected credit losses	Bodies are required to measure at 31 March the loss allowance for a financial instrument at an amount equal to the lifetime expected credit losses (ECLs) if the credit risk has increased significantly since initial recognition. This could mean that ECLs for some financial assets which were previously based on a '12-month' assessment may move to 'lifetime' ECLs. The economic outlook for a body's financial assets as a result of COVID-19 must be taken into account when assessing ECLs. Bodies need to consider the: • risk of default of its financial assets • exposure to that default risk • estimated loss as a result of the default. ECLs will be individual to each body's debt portfolios, the nature of its financial assets held at amortised cost, and the impact of COVID-19 in its local area (as well as national economic events).
Management Commentary	Narrative reporting will need to cover the effects of COVID-19 on services, operations, performance, strategic direction, resources and financial sustainability. Appendix 3 includes a list of issues bodies may wish to consider including: • Issues that have affected service provision • Workforce changes • Impact on the supply chain • Reserve levels and cash flow management • Major risks and recovery plans.

Retirement benefits – 2019/20 report on actuarial information

38. Professional Support has arranged for PWC to provide a report* to support auditors when assessing the competence and objectivity of, and assumptions and approach adopted by, actuaries producing information required by IAS 19 figures in respect of the Local Government Pension scheme (LGPS) as at 31 March 2020.

39. PWC have confirmed the competence and objectivity of the actuaries involved in valuations for the LGPS in Scotland. They also consider that the assumptions proposed, when taken together, will produce liability figures in line with their expectations.

Proposed actuarial assumptions are reasonable in typical cases

40. However, the report advises auditors to consider whether:

- local issues have been adequately covered in instructions issued by employers to actuaries (page 3)
- to subject the source data provided to the actuaries by employers to further audit procedures as discussed in section 4 of the report
- to establish actual asset returns and compare them with expected returns arrived at using market indices (see page 16)

- additional procedures are required for employer bodies advised by Barnett Waddingham as that actuary does not adjust for actual pension increases in their roll forward calculations (see page 20)
- material significant events have been communicated to the actuary and undertake additional audit procedures as appropriate (page 3).

41. Page 24 of the report provides a summary of the approach each actuary is taking for the McCloud judgement. In summary:

- All actuaries confirmed that where an allowance was made in 2018/19, any update to that allowance for 2019/20 would be recognised within Other Comprehensive Income (OCI).
- Most actuaries confirmed that where no allowance was made in 2018/19, an allowance would be made for 2019/20 and recognised as past service cost.
- Hymans Robertson propose to make no allowance in 2019/20 unless instructed by an employer body and are allowing the bodies to choose whether any allowance is recognised in OCI or past service cost.
- Appendix E summarises the approach to calculating the allowance taken by each actuary and highlights that the approach taken by Hymans Robertson is likely to be more approximate than the others. Further testing by auditors may be necessary where Hymans Robertson is the actuary.

Hymans are not making allowances for the McCloud judgement or GMP unless instructed

42. Page 26 of the report provides a summary of the approach each actuary is taking to Guaranteed Minimum Pension (GMP) indexation:

- Most actuaries are making an allowance for full GMP indexation for members with a statutory retirement age after April 2016.
- Hymans Robertson are giving employing bodies the option to make this allowance.

43. Auditors should refer to paragraphs 20 to 32 in Module 4 of Technical Guidance Note 2019/10(LG).

Grant income - funding scheme

44. The Scottish Government has issued a number of finance circulars setting out the conditions for a Business Support Fund grant scheme administered by councils that is designed to help eligible businesses during the COVID-19 crisis. The two funds within the scheme are:

- Small Business Grant Fund (SBGF)
- Retail, Hospitality and Leisure Grant Fund (RHLGF).

45. An application requires to be completed for receipt of the grant. There have to date been the following three phases of the scheme:

- Phase 1 commenced on 18 March 2020. Finance Circular 8/2020 sets out the conditions for the first phase. Each ratepayer registered the day before the scheme started could claim one grant, regardless of how many properties they had.
- Phase 2 commenced on 5 May, and Finance Circular 9/2020 expands the ways in which RHL businesses can access the SBGF. Following the initial one-off grant, each additional eligible property qualifies for a grant equal to 75% of the one-off grant.
- Phase 3 commenced on 8 June, and Finance Circular 11/2020 also enhances accessibility to the SBGF, including extending the scope to tenants who are not the rate payer for the property.

46. Eligibility criteria and other Information in respect of each fund in the scheme are summarised in the following table:

Feature	SBGF	RHLGF
Payment on first property	£10,000	£25,000
Payment for additional properties (phases 2 and 3)	£7,500	£18,750

Feature	SBGF	RHLGF
Use eligibility	Property must have been wholly or mainly used for one of the qualifying purposes set out in Table 1 in 8/2020 (or similar purpose). Properties used for the purposes set out in Table 2 are specifically excluded.	Property must be operating in the retail, hospitality or leisure sectors and must be used for one of the qualifying purposes set out in Table 3 (or similar purpose).
Relief eligibility (phase 1)	Property must be in eligible for the Small Business Bonus Scheme or Rural Relief.	N/A
Relief eligibility (phase 2)	As for phase 1 plus RHL businesses ineligible for either fund with a cumulative rateable value of all properties between £35,001 and £51,000	N/A
Relief eligibility (phase 3)	As for phase 1 plus RHL businesses ineligible for either fund with a cumulative rateable value of all properties between £35,001 and £500,000	N/A
Rateable value	N/A	Individual properties must have a rateable value between £18,001 and £51,000.

47. The property use, reliefs and rateable value of the property are those as at 17 March 2020.

Advice to auditors

48. The following table summarises a selection of requests for technical advice recently made by auditors to Professional Support in respect of the audit of the 2019/20 annual accounts of local government bodies, along with the advice offered:

Auditor Action
Auditors should consider the application of this advice to their own audits

Property, plant and equipment

Can employee costs be capitalised if the employees have been redeployed from a planned capital project as a result of COVID-19?
Costs attributable to bringing an asset to the location and condition necessary for it to be capable of operating in the manner intended by the public body can be capitalised (i.e. included in the cost of the asset rather than being charged to revenue). Employee costs should be capitalised only where the employee's activities are directly attributable. If an employee has been diverted onto other duties, their salary for the duration of those duties cannot be capitalised.

Can employee costs continue to be capitalised if work already carried out on a project requires to be carried out again due to delays?
If the costs of an activity related to an asset are capitalised but then for whatever reason that activity has to be carried out again, only the costs related to the second occasion can be capitalised. In the scenario where an employee carried out work on a project but due to delays the work has to be carried out again, the council would have to reverse the entire amount capitalised to date back out to revenue as soon as they realise the costs will need to be incurred again.

Loans fund

Should a change in the method for calculating loans fund repayments be applied retrospectively

Finance Circular 7/2016 is clear that changing from the statutory method to a prudent method of calculating the repayments represents a change in accounting policy. Changes in accounting policy are normally applied retrospectively unless there are specific transitional provisions. Finance Circular 7/2016 also states that the change in accounting policy should be applied prospectively, i.e. in respect of repayments from the date of change.

Housing Revenue Account

Does a council have the statutory power to charge maintenance costs to its Housing Revenue Account (HRA) if no maintenance is actually being carried out due to COVID-19 suppression measures?

The credit and debit items required to be made to the HRA are set out schedule 15 of the Housing (Scotland) Act 1987. Schedule 15 states that a "local authority shall debit to the housing revenue account amounts equal to ……the expenditure incurred by the local authority for that year in respect of the repair, maintenance, supervision and management of houses and other property to which the account relates".

Some councils charge staff costs directly to the HRA while others have a corporate property maintenance function and an element is recharged to the HRA. Councils should seek their own legal advice if in doubt, but the following sets out the views of Professional Support:

There is no objection to a council continuing to charge staff costs directly to the HRA. The expenditure is still being incurred even if the repair activities cannot actually be carried out at the moment. The alternative of instead charging the staff costs to the General Fund does not seem fair or reasonable.

Similarly, the costs of a corporate property maintenance function should also continue to be recharged to the HRA on a fair and reasonable basis. There may be an apparent complication if a council chooses to run the property maintenance function as an internal trading operation and charges the HRA for services provided. Such charges are for internal purposes and do not impact on the recharge to the HRA for external financial reporting purposes.

There should not be any difference regardless of whether councils charge the HRA directly or indirectly.

Statutory Other Information developments

Revised statutory guidance on Management Commentary

49. Finance Circular 10/2020 also contains statutory guidance in respect of the contents of the Management Commentary. The statutory guidance permits, but does not require, a local government body to disapply the following content requirements for the Management Commentary:

- The requirement for the review of the body's business to be comprehensive.
- An analysis using key performance indicators (KPIs). However, a hyperlink to KPIs published elsewhere is required or a statement that is not possible.
- A description of the body's strategy and business model. However, a hyperlink to a document published elsewhere is required or a statement that is not possible.
- Political donations and expenditure, financial instruments, indication of future likely developments, disclosure concerning the employment of disabled persons, employee involvement, and disclosures concerning greenhouse gas emissions.
- The requirement to direct the reader to the annual report on treasury management to the extent that the report is not yet published. However, a statement to that effect should be included.

The content requirements for the Management Commentary have been varied

50. Professional Support has revised Module 11* of Technical Guidance Note 2019/9(LG) to reflect the statutory guidance on the Management Commentary.

Grant claims developments

Technical guidance notes for 2019/20

51. Professional Support has published Technical Guidance Note TGN/GEN/20 Auditor Certification of 2019/20 Approved Local Government Grant Claims and Returns to provide general guidance to auditors on the certification of 2019/20 local government grant claims and returns and to explain the approach and procedures to be adopted. The TGN:

- explains the arrangements for the certification of grant claims and other returns
- provides a list of grant claims and other returns which external auditors are required to certify in 2019/20 under their audit appointment
- considers the roles and responsibilities of Professional Support, grant-paying bodies, local government bodies, and appointed auditors
- sets out the overall approach to be adopted by auditors
- provides guidance on auditor reporting.

52. Professional Support also separately publishes a separate TGN on each significant approved claim to provide auditors with specific guidance on certifying that claim. The following have been published for 2019/20:

- Technical Guidance Note TGN/BEL/20 Auditor certification of 2019/20 Bellwin Scheme of Emergency Financial Assistance to Local Authorities
- Technical Guidance Note TGN/HBS/20 Auditor Certification of 2019/20 Housing Benefit Subsidy Claims
- Technical Guidance Note TGN/EMA/20 Auditor Certification of 2019/20 Education Maintenance Allowance Claims
- Technical Guidance Note TGN/NDR/20 Auditor Certification of 2019/20 Non-Domestic Rates Income Return.

Auditor action
Auditors should use these TGNs when certifying 2019/20 grant claims

Housing benefits

53. The Department for Work and Pensions (DWP) has issued the Module 5 software diagnostic tool component of the HBAP approach to the certification of the 2019/20 housing benefit (HB) subsidy claims as well as:

- HB Circular A7/2020 to advise of changes to the additional earnings disregard for housing benefit purposes
- HB Circulars S4/20, S5/20, S6/20 and S7/20 to announce additional funding.

Non-domestic rates

2019/20 return

54. The Scottish Government has issued the 2019/20 return and accompanying guidance notes for non-domestic rates. The most significant changes from 2018/19 are summarised in the following table:

Line	Relief	Change
18 and 19	Transitional	The scheme for some business sectors following the revaluation exercise applicable from 1 April 2017 has been extended to 2019/20
21a and 21b	Business Growth Accelerator	Separate reporting of Business Growth Accelerator relief for improved property (line 21a) and new property (lines 21b)
24	New Fibre	New 100% relief to any provider of new fibre infrastructure for telecommunication
25	Lighthouse	Separate reporting

Line	Relief	Change
28 and 29	Sports Clubs	Separate reporting of discretionary relief for Community Amateur Sports clubs (CASCs) or sports clubs which are registered charities (line 28) from other sports clubs (line 29)
40,41 and 43	Backdated	Separate reporting of backdated sports and charities relief (line 41), backdated Business Growth Accelerator relief (line 40) and other backdated relief (line 43)

Whole of Government Accounts developments

2019/20 guidance

55. HM Treasury has issued guidance for local government users on the 2019/20 Data Collection Tool for Whole of Government Accounts (WGA).

56. A key refinement is that bodies will be able to run the counterparty Matches Report themselves and will be able to see live published data from other bodies for easier rectification of counterparty transactions.

Wider audit scope developments

Treasury and capital management update

57. CIPFA has issued Bulletin 4 Treasury and Capital Management Update to provide an update on treasury management and capital management issues. Paragraphs 4 to 11 of the bulletin set out a number of key issues which need to be considered as a result of COVID-19. They include the following:

- Day-to-day cash flow management should be prioritised. Bodies should consider the control systems required to gather as much information as possible on significant inflows and outflows, such as:
  - the timing for likely changes to the major schemes in the capital programmes
  - the impact of COVID-19 on service provision and cash collection, or new or different levels of grant
  - overtime or special arrangements for key workers.
- Bodies should keep under review the liquidity of their investment portfolios and make cash available in the shorter term. They may also need to consider their ability to be able to convert investments to cash at short notice and even the liquidity of their longer-term investments.
- Borrowing may need to be higher in the short or medium term than originally planned, and may potentially be in excess of agreed limits. Paragraph 29 of the Prudential Code allows bodies to respond to unforeseen and extraordinary circumstances.
- Bodies should consider the procedures in place to ensure that treasury management teams can operate day to day operations remotely.

Guidance on financial management code

58. CIPFA has issued guidance notes* to assist local government bodies in complying with the Financial Management Code referred to in Technical Bulletin 2019/4 (paragraph 54). The notes:

- explore the themes addressed in the code
- provide suggestions as to how it can be implemented in practice
- suggest how bodies might demonstrate that compliance with the code has been achieved.

Summary of auditor actions in this section

Paragraphs	Auditor actions
17 -22	Use Technical Guidance Note 2020/5(LG) when reporting the audit of the 2019/20 annual accounts and complete the checklist
43	Consider the application of the advice from Professional Support to their own audits

Paragraphs	Auditor actions
46 - 47	Use the applicable TGN when certifying 2019/20 grant claims

Contact points for this section

59. The contact points for this section of the Technical Bulletin are:

- Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk
- Anne Cairns, Manager (Professional Support) – acairns@audit-scotland.gov.uk (grant claims items only).

Section 3

Central government sector

Statutory Other Information developments

Addendum to 2019/20 FReM

60. HM Treasury has issued an addendum to the 2019/20 FReM to set out minimum reporting requirements for the annual report and accounts as a result of the impact of COVID-19 suppression measures.

61. The addendum permits, but does not require, bodies to omit the performance analysis section from the Performance Report. Where relevant performance information has already been published elsewhere, bodies are encouraged to refer to the relevant publication.

The performance analysis section may be omitted

62. Where unaudited information otherwise required to be included in the Accountability Report is already published elsewhere, bodies are permitted to refer to the relevant publication rather than including the information in their Accountability Report.

63. Professional Support has revised Module 11* of Technical Guidance Note 2020/1 to reflect the impact of the FReM addendum.

Advice to auditors

64. The following table summarises a selection of requests for technical advice recently made by auditors to Professional Support in respect of the audit of the 2019/20 annual accounts, along with the advice offered:

Auditor action
Auditors should consider the application of this advice to their own audits

Leases and similar arrangements

How should a rent-free period be accounted for in an operating lease?
A rent-free period is an incentive for the lessee to enter into the lease agreement. Bodies are required to recognise lease incentives in accordance with SIC 15 Operating Lease – Incentives as a reduction in the lease expense over the lease term on a straight-line basis (unless another systematic basis is more representative of the benefits received by the body).

Intangible assets

Should software licences be recognised as intangible assets?
IAS 38 defines an intangible asset as an identifiable non-monetary asset without physical substance which should be recognised if (and only if) it is controlled by the body as a result of past events, and future economic or service benefits are expected to flow from the asset to the body. Software licences allow the body to use the software for a specified period. Where this is for a period in excess of 12 months, the licence will provide future service potential and may be recognised as an intangible asset.

Remuneration and Staff Report

Should all "directors" be disclosed within the Remuneration and Staff Report?
The FReM requires information to be disclosed in the Remuneration and Staff Report for each director. For the purposes of this disclosure, it describes directors as the management board (including advisory and non-executive members) having authority or responsibility for directing or controlling the major activities of the body during the year. It will not necessarily include an individual simply because they have 'director' in their job title. Similarly, it may include individuals who do not have 'director' in their job title. Disclosure is determined by the role undertaken by the individual. Bodies will have to consider whether the individual role meets the definition in the FReM. For example, a director of IT with a role limited to the delivery of a specific IT project is unlikely to meet the definition.

Should employer's pension contributions be included in a director's remuneration in the Remuneration and Staff Report?
The employer's contribution is not included within a director's remuneration. It is effectively reflected in remuneration in the value of pension benefit column, as this is the increase in pension benefit that was purchased with the employer's contribution.

Auditing developments

2019/20 model independent auditor's reports

65. Professional Support has published Technical Guidance Note 2020/4(CG) 2019/20 Independent Auditor's Report for Central Government Bodies to provide auditors with the model Independent Auditor's Reports which should be used for the 2019/20 annual report and accounts.

66. The model Independent Auditor's Reports set out in Appendices 1 to 4 of the TGN have been tailored to reflect central government legislation and augmented by the reporting requirements of the Auditor General. There have been no significant changes to the model Independent Auditor's Reports for 2019/20.

67. The TGN also provides guidance on the amendments that require to, or may, be made to the wording in the models in the form of auditor actions. Some enhancements have been made to the guidance to make the required auditor actions clearer. Auditors should complete for each report the checklist at Appendix 5 which provides a list of those auditor actions.

68. Any proposed modifications to any audit opinion or conclusion, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with Professional Support in advance of finalising the report.

69. Auditors should use this TGN when reporting on 2019/20 audits.

Auditor action

Auditors should use this TGN when reporting the audit of the 2019/20 annual report and accounts and complete the checklist

Whole of Government Accounts developments

2019/20 guidance

70. HM Treasury has issued guidance for local government users on the 2019/20 Data Collection Tool for Whole of Government Accounts (WGA).

71. A key refinement is that bodies will be able to run the counterparty Matches Report themselves and will be able to see live published data from other bodies for easier rectification of counterparty transactions.

Summary of auditor actions in this section

Paragraphs	Auditor actions
57	Consider the application of the advice from Professional Support to their own audits
58 - 62	Use Technical Guidance Note 2020/4(CG) when reporting the audit of the 2019/20 annual report and accounts and complete the checklist

Contact point for this section

72. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 4

Health sector

Annual report and accounts developments

Guidance on 2019/20 accounts

73. The Technical Accounting Group (TAG) has issued additional guidance* on the expected impact of COVID-19 suppression measures on the 2019/20 annual report and accounts of health boards.

74. The guidance advises that, where a board omits the performance analysis section of the Performance Report, specific disclosures required by the accounts manual (i.e. on financial targets and payment policy) should be included within the performance overview section.

75. All areas of the financial statements will be required. However, the guidance advises boards to engage with auditors to consider the appropriateness of excluding or reducing detail in notes to the financial statements where the disclosure is not material.

76. It is expected that additional disclosures will be required to reflect market uncertainties and the impact on asset valuations at 31 March. A suggested form of words is included at paragraph 16 of the guidance. There is also a suggested disclosure at paragraph 22 on the deferral of the application of IFRS 16.

Disclosure wording is suggested

77. The guidance highlights other areas where further disclosure may be required including:

- credit or liquidity risk disclosures for financial instruments
- year-end inventory, particularly where planned counts were unable to be performed
- income and expenditure where there is a high level of estimation, or material movement from previous years

78. The guidance also advises that the threshold for tolerance used in the agreement of balances between boards has been raised to £500,000

Submission timetable

79. In line with the rest of the UK, the Scottish Government has delayed the administrative deadlines for the annual report and accounts of health boards by three months. Boards are required to submit draft accounts by the end of August and audited annual accounts by the end of September.

80. However, some boards have indicated that they intend to proceed with accounts preparation in line with normal timescales.

Provisions for clinical negligence claims

81. Professional Support has issued a report* to auditors following an examination of the Clinical Negligence and Other Risks Indemnity Scheme (CNORIS). The purpose of the report is to:

- provide assurance on the methodology used by the Scottish Government in the calculation of the CNORIS national obligation at 31 March 2020
- inform auditors' evaluation of the role of the NHS Central Legal Office as a management expert.

Auditor action
Auditors should refer to this report when auditing the 2019/20 provision for CNORIS

Auditor action
Auditors should consider the application of this advice to their own audits

Advice to auditors

82. The following table summarises a selection of requests for technical advice recently made by auditors to Professional Support in respect of the audit of the 2019/20 annual report and accounts, along with the advice offered:

Grants and other income

Should a liability be recognised for internal recharges relating to research and development income?
In accordance with generally accepted accounting practices, a liability should be recognised only in respect of the elements of income from research and development (R&D) contracts that are due to be paid to external partners (e.g. universities). Any internal recharges (e.g. reallocation to a different budget head within a board) should not be recognised in the balance sheet. There may be confusion as the NHS TAG guidance on R&D income could be read as suggesting that amounts due to other budget heads should be included in the liability. Professional Support considers that this was not TAG's intention but in any event the guidance does not supersede generally accepted accounting practice.

Remuneration and staff report

Should the median calculation in the fair pay disclosure in the Remuneration and Staff Report include agency staff costs?
Health boards are required to make the fair pay disclosure because it is a requirement of the accounts manual. The accounts manual is clear that agency staff are excluded from the calculation of median pay. This is because they are not employees on the payroll and instead their service is charged for by invoice. Professional Support acknowledges that this contrasts with the FReM which requires agency staff to be included in the median pay calculation. However, the provisions in the FReM in respect of the fair pay disclosure do not apply in Scotland as (in accordance with FReM paragraph 5.1.4) they do not originate in accounting standards or Companies Act.

How should a negative pension benefit value be treated in the Remuneration and Staff Report?
The increase in value of pension benefit is a component of the total remuneration figure. Where the calculation results in a negative value, the accounts manual requires the value to be expressed as zero in the relevant column in the remuneration table. Negative values do not therefore reduce the total remuneration figure.

Governance Statement

Can a board adjust its membership as a result of the current COVID 19 crisis?
The Health Boards (Membership and Procedure) (Scotland) Regulations 2001 set the quorum for board meetings as one third of the total number of members including at least two members who do not also hold the position of Chief Officer, Chief Finance Officer or Director of Public Health. While it may be appropriate for boards to introduce streamlined governance arrangements during the COVID 19 suppression measures, they should ensure that these arrangements satisfy the requirements of the regulations and are set out in revised standing orders. Amended arrangements should be disclosed in the Governance Statement. Auditors may want to confirm that amended arrangements for board meetings meet the requirements of standing orders and the Regulations, and should evaluate whether amended arrangements are disclosed in the Governance Statement.

Summary of auditor actions in this section

Paragraphs	Auditor actions
72	Use the report provided by Professional Support when auditing the 2019/20 provision for CNORIS
73	Consider the application of the advice from Professional Support to own audits

Contact point for this section

83. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 5

Fraud and irregularities

Auditor action

Auditors should consider whether weaknesses in internal control which facilitated each fraud may exist in their bodies and take the appropriate action

84. This section contains a summary of fraud cases and other irregularities facilitated by weaknesses in internal control at audited bodies that have recently been reported by auditors to Professional Support.

Expenditure

Invalid supplier

85. A third party defrauded £64,500 from a public sector body by purporting to be a genuine supplier.

Key features

The purchase ledger team received several emails purporting to be from a named contact at their utility supply company requesting payment of legitimate outstanding invoices. They included copy invoices from the supplier which appeared to be genuine. The emails requested that the standing bank details be amended to those on the invoices. The bank details were changed, and three payments were made. Remittance advices were sent to the legitimate supplier email address. The fraud was identified when correspondence from the legitimate contact in the supplier was received advising that they had received remittance advice notices but no payment.

The fraud was possible as the procedure for confirming bank account changes was not followed. In addition, the email from the supplier had a subtle difference in the address that was not identified at the time.

All finance staff are now receiving training on fraud prevention and detection.

Police Scotland have been informed.

Payroll

Re-directing salary

86. A third party defrauded over £5,000 from a council by re-directing salary payments.

Key features

The payroll team received an email purporting to be from a senior officer of the council, requesting a change to bank account details. The payroll records were amended, and a salary payment was made.

It was not identified as fraud until the officer contacted the payroll team to query why they had not been paid.

The fraud was possible as the procedures in place to check the validity of bank detail changes had not been followed.

Payroll staff have been reminded of the proper verification procedure for changes to employee bank account details. They have also received refresher training on how to spot fraudulent emails. The case is being investigated by Police Scotland.

Contact point

87. The contact point for this section of the Technical Bulletin is Anne Cairns, Manager (Professional Support) – acairns@audit-scotland.gov.uk.

Technical Bulletin 2020/2

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or **info@audit-scotland.gov.uk**

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Technical Bulletin 2020/3

Technical developments and emerging risks from July to September 2020

Prepared for appointed auditors and audited bodies in all sectors

22 September 2020

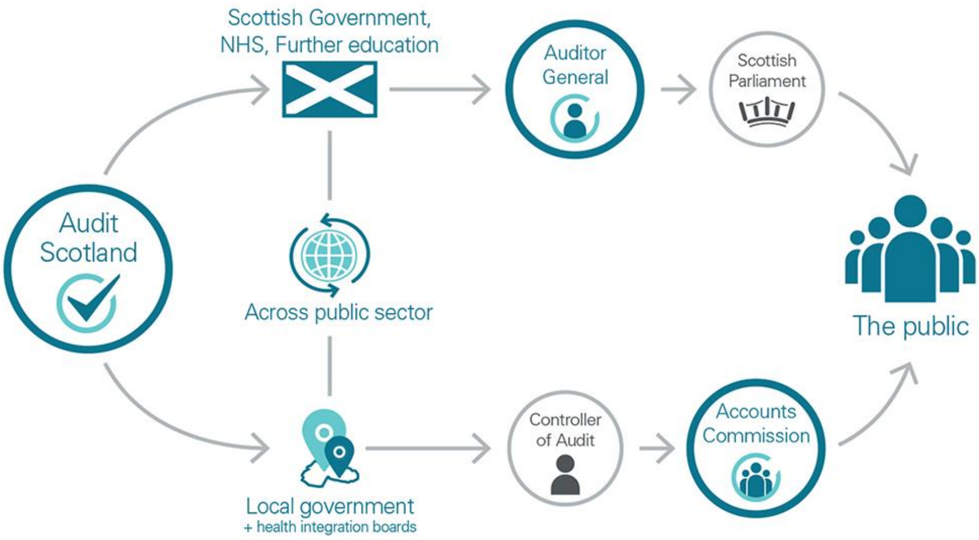
Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.

- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.

- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money

- reporting our findings and conclusions in public

- identifying risks, making clear and relevant recommendations.

Contents

Introduction

Purpose

1. The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector and on professional matters during the quarter
- guidance on any risks of misstatement emerging in the quarter.

Technical Bulletins provide information on developments and guidance on emerging risks

2. Appointed auditors are required to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require to be aware of. It may still be necessary for auditors to read the source material if greater detail is required. These can be accessed by using the hyperlinks. They are also available from the Technical Reference Library* maintained by Professional Support.

3. The actions by auditors recommended by Professional Support in respect of each item are highlighted in red and are also summarised at the end of each section.

4. Technical Bulletins are also published on the Audit Scotland website and therefore are available to audited bodies and other stakeholders. Hyperlinks indicated with an asterisk link to the Technical Reference Library and therefore are active only for auditors.

Highlights summary

5. Professional Support draws attention in the following table to certain items in this Technical Bulletin:

Professional Support has provided technical advice to auditors on a number of issues [see paragraphs 7, 47, 49, and 51]	CIPFA/LASAAC has issued the 2020/21 accounting code for local government[see paragraph 8]	CIPFA/LASAAC has issued the draft 2021/22 accounting code [see paragraph 21]
The SPPA has issued the proposed remedy to the McCloud judgement [see paragraph 27]	The SPPA has issued a circular on the Goodwin tribunal [see paragraph 32]	A recent judicial review ruling impacts on the structures built on common good land [see paragraph 35]
Professional Support has published guidance on risks of misstatements in the 2019/20 annual report and accounts of colleges [see paragraph 53]	Professional Support has published model 2019/20 Independent Auditor's Reports for colleges [see paragraph 57]	The SFC has issued the 2019/20 Accounts Direction for colleges [see paragraph 61]
The SFC has issued guidance on the 2019/20 financial statements of colleges [see paragraph 64]	The FRC has a issued a revised auditing standard on risks of material misstatement [see paragraph 67]	The FRC has issued a report on the financial reporting effects of COVID-19 [see paragraph 70]

Contact point

6. The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – pobrien@audit-scotland.gov.uk.

Feedback on this Technical Bulletin is welcome

Section 1

Cross sector

Auditor Action
Auditors should consider the application of this advice to their own audits

Advice to auditors

7. The following table summarises requests for technical advice made by auditors to Professional Support during the quarter in respect of the audit of the 2019/20 annual accounts which applies to all public bodies, along with the advice offered:

Property, plant and equipment

A body has replaced a section of the roof of a building. Should the cost of the replaced section be capitalised?

The appropriate treatment depends on whether the replaced section is being treated (i) as a separate component or (ii) as part of an asset (e.g. the asset is the whole roof or indeed the building itself).

Where the replaced section is a separate component, it is relatively straight-forward. The cost can be capitalised as follows:

- The replaced section is derecognised. If the original cost of the roof is not known, it should be estimated.
- The cost of the new section is capitalised and treated as a separate asset.
- The new section/asset is depreciated over its own useful life.

Where the replaced section is part of an asset, further consideration is required. The first question is whether the work was undertaken to repair damage to the roof. If that is the case, the cost of the work can be capitalised as follows:

- The damage means the asset was impaired and therefore an impairment loss should have been recognised (and consequent reduction in the carrying amount of the asset).
- The cost of the new section is capitalised and added to the carrying amount of the asset.

If the work was not to repair damage, the question is whether the work has added to the service potential (or economic benefits) of the asset (e.g. by increasing the expected useful life). Expenditure can be included in the carrying amount of an asset (i.e. capitalised) if the expenditure has added to the future economic benefits or service potential of the asset. Where the work undertaken maintains the existing service potential (e.g. it is part of maintenance programme that was assumed when the expected useful life was originally estimated), the cost should be recognised as an expense.

Should a body be carrying out an impairment review of its office buildings at 31 March 2020?

IAS 36 Impairment of Assets sets out indications that an asset is impaired. This includes where significant changes with an adverse effect on the body have taken place during the period regarding the extent to which an asset is used. These changes include the asset becoming idle.

As most offices were not in use at 31 March 2020 due to coronavirus disease 2019 (COVID-19) suppression measures, it is likely they were impaired and it would be appropriate to obtain a valuation.

Summary of auditor actions in this section

Paragraph	Auditor actions
7	Consider the application of the advice from Professional Support to own audits

Section 2

Local government sector

Financial statements

2020/21 accounting code

8. The CIPFA/LASAAC Local Authority Code Board (CIPFA/LASAAC) has issued the Code of Practice for Local Authority Accounting in the UK* (the accounting code) which sets out local government accounting requirements for 2020/21.

9. The accounting code's financial reporting framework is based on International Financial Reporting Standards (IFRS) as adopted by the European Union, adapted for the local government context where necessary. The 2020/21 accounting code has been prepared on the basis of accounting standards and other pronouncements in effect for accounting periods commencing on or before 1 January 2020 (except for IFRS 16 Leases which has been deferred to 2021/22).

10. The changes in the 2020/21 accounting code are summarised in its Foreword. They include the following changes that Professional Support draws auditors' attention to:

- Amendments to reflect changes to the definition of material.
- The implementation of amendments to IAS 19 Employee Benefits.
- Amendments to accounting and reporting by pension funds.
- Amendments relating to financial instruments.
- The total line in Comprehensive Income and Expenditure Statement.

Amendments to reflect changes to the definition of material

11. The wording of the definition of material at paragraph 2.1.2.15 has been amended in line with an amendment to IAS 8. It now states that information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that users make on the basis of those financial statements.

Definition now includes obscuring information

12. The main change in the definition is the reference to the concept of obscuring information. Paragraph 2.1.2.15 has therefore been added to explain that information regarding a material item may be obscured if, for example:

- the language used is vague or unclear
- information is scattered throughout the financial statements
- items are inappropriately aggregated or disaggregated
- a material item is hidden by immaterial information.

13. Paragraph 2.1.2.16 has also been added to advise that judgement is required regarding the extent of supporting disclosures that are appropriate for a specific item. In particular, the materiality of an item in a primary statement does not include a presumption that all supporting information disclosures specified in the accounting code for that item are material. This applies for both descriptive and numerical supporting information.

14. In addition, paragraph 2.1.2.17 states that judgements regarding materiality should be based on the needs of users. Additional information may be disclosed where this does not obscure information that is material for users.

Implementation of amendments to IAS 19

15. Paragraph 6.4.3.5 has been added as a result of an amendment to IAS 19. It creates an exception to the rule that financial assumptions are based on market expectations at 31 March.

16. Where a pension scheme amendment, curtailment or settlement occurs during the year the amended assumptions, as used for the remeasurement of the net defined benefit liability, are to be applied in relation to the benefits for the remainder of the year.

Amendments to accounting and reporting by pension funds

17. The following changes have been made to align with the SORP for pension funds:

- The disclosure requirement for pooled investment vehicles in the net assets statement (paragraph 6.5.3.6) has been amended to require an analysis between equities, bonds, property, hedge funds, diversified growth funds, private equity funds, infrastructure funds and other.
- The previous requirement (at paragraph 6.5.5.1) for an analysis of investment assets between 'UK' and 'overseas' and between 'quoted' and 'unquoted' has been removed.

Amendments relating to financial instruments

18. Amendments related to financial instruments are summarised in the following table:

Paragraph	Amendment
3.4.2.39(c)	Gains and losses on financial instruments classified as fair value through profit or loss have been added to the items included in the financing and investment income and expenditure line of the Comprehensive Income and Expenditure Statement.
7.2.9.1	Clarification has been added regarding the extent of the exemption from recognising a loss allowance for expected credit losses on a financial asset where the counterparty is central government. It has been clarified that the exemption does not apply to: • credit impaired assets • NDPBs unless explicitly covered by a guarantee given by their sponsor department.
7.1.1.3(c)	Clarification has been added in respect of the application of the interpretation of IFRS 9 that the options that characterise clauses within a LOBO contract should not be separately accounted for. It has been clarified that this interpretation only applies where the specified derivative elements are separable. It does not apply to a compound embedded derivative if separation of the exempted derivative is not permitted by IFRS 9.
7.1.1.3(e)	Clarification has been added that the modification of financial liabilities follows the principles specified for the modification of financial assets, i.e. when the change in terms is not substantial, it is not accounted for as an extinguishment.
7.1.6.4	The wording of the definition for a soft loan has been amended to include loans where the interest rate is specified at below zero (i.e. negative interest).

Comprehensive Income and Expenditure Statement total line

19. A footnote has been added to paragraph 3.4.2.39 in respect of the total comprehensive (income) and expenditure' line in the Comprehensive Income and Expenditure Statement. It requires the line description used to provide clarity regarding the use of positive and negative signage. For example, where brackets are used to represent an overall surplus the description 'Total comprehensive (income) and expenditure' may be used.

IFRS 16

20. Appendix F has been added to the accounting code to set out the provisions in respect of IFRS 16 Leases that are anticipated to be included the 2021/22 accounting code. The appendix is intended to provide advanced notification of the requirements. Early adoption of IFRS 16 is not permitted.

Draft 2021/22 accounting code

21. CIPFA/LASAAC has issued a consultation paper on the accounting code for 2021/22. The main issues in the consultation are in respect of:

- the application of specific aspects of IFRS 16 Leases

- CIPFA/LASAAC's strategic plan to improve the clarity of the accounting code.

22. Responses should be sent to cipfalasaac@cipfa.org by 23 October 2020.

Application of specific aspects of IFRS 16 Leases

23. The consultation includes three areas relating to the adoption of IFRS 16 which require further consideration. They are summarised in the following table:

Area	Consideration
Service concession arrangement liability	Exposure draft B sets out proposals for measuring a service concession arrangement liability on the basis of IFRS 16. However, the consultation paper asks for views on the alternative of continuing to use IAS 37. It also asks whether any move to use IFRS 16 should be in 2021/22 or 2022/23.
Leases at a peppercorn rate or nominal amount	The adoption of IFRS 16 currently includes an interpretation where assets which are leased for nil consideration, a nominal amount, or at a peppercorn rate are treated as being analogous to donated assets. The consultation asks for views on whether the interpretation is appropriate for a lease at a peppercorn or nominal lease payment where the contractual arrangements are on commercial terms.
COVID-19-related rent concessions	An amendment to IFRS 16 provides lessees with an exemption (as a practical expedient) from assessing whether a COVID-19-related rent concession is a lease modification. It is proposed to allow local government bodies to apply the practical expedient on transition to IFRS 16.

24. A fourth area related to the treatment of housing revenue account tenancy agreements under IFRS 16 will be subject to a separate consultation paper.

Strategic plan to improve clarity

25. As part of CIPFA/LASAAC's strategic plan to improve clarity, the consultation asks for views on the following aspects of the accounting code:

Aspect	Request for views
Summary of taxpayers funding	The option to include a summary of taxpayers' funding in the narrative report
Comprehensive Income and Expenditure Statement	Whether reporting of financial performance in the Comprehensive Income and Expenditure Statement could be improved
Expenditure and Funding Analysis Note	Comments on the role of the Expenditure and Funding Analysis and whether any improvements are required
Capital accounting	Whether the application of materiality to the disclosure requirements would benefit from a review
Pensions accounting	Whether the application of materiality to the disclosure requirements would benefit from a review
Financial instruments	Whether the reporting requirements are excessive
Group accounts	Comments on the usefulness of group accounts to the users of the financial statements

Other issues

26. Other issues raised in the consultation are summarised in the following table:

Area	Paragraphs	Consideration
Redmond Review	11 to 14	There is a request for views on the impact of the recommendations in the Redmond Review on local authority financial reporting (referred to later at paragraph 39).
Interest Rate Benchmark Reform Phase 2: Amendments	50 to 55 and Exposure Draft C	Interest rate benchmarks such as interbank offered rates underpin many financial products. The amendment to IFRS 9 and other affected standards has been issued as part of the ongoing reform of interest rate benchmarks across the world. There are proposals that local government bodies should apply the amendments to IFRS 9 for changes in the basis for determining the contractual cash flows of a financial asset or financial liability as a result of interest rate benchmark reform.
Estimation uncertainty disclosures	62 to 66 and Exposure Draft D	There is a proposal that the requirements of the accounting code in respect of disclosing estimation uncertainty be augmented by referring bodies to paragraphs 126 to 127 and 129 of IAS 1. These paragraphs cover, for example, the estimation of the effects of uncertain future events, and provide examples of the types of disclosures where estimation uncertainty might apply.
IFRS 17 Insurance Contracts	71 to 78	Last year's consultation identified some local government practices that may come within the scope of IFRS 17. They are listed at paragraph 77 of the Invitation to Comment and include pension guarantees, and mutual insurance arrangements. This year, views are being requested on the types of arrangements listed, whether any others missing from the list and the incidence of such transactions.

Proposed remedy for McCloud judgement on pensions

27. The Scottish Public Pensions Agency (SPPA) has issued a consultation paper setting out the proposed remedy to the age discrimination provisions in the Local Government Pension Scheme (LGPS) highlighted by the McCloud and Sargeant judgements. These judgements found that transitional protections for certain members on moving from the 2009 to 2015 schemes discriminated against younger members on the grounds of age.

28. Transitional provisions provided members who were within 10 years of normal retirement age in 2012 with a statutory underpin. The underpin provided those members with benefits under either the 2009 scheme or 2015 scheme, depending on which was better. The proposed remedy is to offer the same underpin to all members of the 2015 scheme until 2022.

29. Comments on the proposed remedy should be sent to SPPAPolicy@gov.scot by 23 October 2020.

30. The issue of the consultation paper provides evidence of conditions that existed at 31 March 2020 and therefore should be treated as an adjusting event after the year end. Auditors should evaluate whether bodies consider, in discussion with their actuaries, whether the impact on estimates of pension liabilities at 31 March 2020 resulting from this information is material and therefore whether an adjustment is required. Professional Support is aware that some actuaries are already offering to provide revised reports while others do not believe this will be necessary.

31. Where the impact is not material and an adjustment to the liabilities is not made, there is no need for the body to make a disclosure to that effect.

Auditor Action

Auditors should evaluate whether bodies are considering the impact on pension liabilities

Circular on the Goodwin tribunal

32. The SPPA has issued circular 2020/04 to advise of changes to the LGPS as a result of the outcome of a recent employment tribunal (the Goodwin tribunal). The circular advises that there are changes to the pension entitlement of male survivors in opposite sex marriages to take into account the female member's service from 6 April 1978. Previously, the male spouse survivor's entitlement was based on service accrued from 6 April 1988.

Auditor Action
Auditors should evaluate whether bodies are considering the impact on pension liabilities

33. The change is backdated to 5 December 2005. The change therefore affects the pension of male spouse survivors where their entitlement arose (i.e. where the female member died) on or after 5 December 2005.

34. Auditors should evaluate whether bodies are considering, in discussion with their actuaries, whether the impact on pension liabilities at 31 March 2020 resulting from this tribunal is material and therefore whether an adjustment is required.

Judicial review on common good assets

35. A recent judicial review ruling* impacts on common good land and the structures built on it. The case under review related to a leisure centre built by a council on common good land. The council no longer uses the building and wanted to demolish it.

36. The ruling determined that buildings on common good land are generally considered to be part of the land and the title which relates to it. This would mean that legal title of such buildings rests with the common good. This includes any buildings constructed by the council on common good land.

Buildings on common good land belong to the common good

37. Although the title to the building rests with the common good, in Professional Support's view, that does not necessarily mean that it should be recognised as an asset on the common good balance sheet. Where a council uses the building to deliver a service, it may be that the council is in substance effectively leasing the asset from the common good. Where the arrangements represent a finance lease, the asset would be recognised on the council balance sheet.

38. The ruling also means that, before a council can dispose of the building or change its use, it would have to follow the consultation provisions under section 104 the Community Empowerment (Scotland) Act 2015.

Report from the Redmond Review

39. Sir Tony Redmond has issued a report following his review into the local audit of, and financial reporting by, local authorities in England.

40. The report recommends in respect of local audit in England:

- the creation of a new regulatory body called the Office of Local Audit and Regulation responsible for the procurement, contract management, regulation, and oversight of local audit
- revision of the current fee structure to ensure adequate resources are deployed
- extending the deadline for published audited annual accounts from 31 July to 30 September.

41. In respect of financial reporting for local authorities in England, the main recommendation is that a simplified statement of service information and costs is prepared by each local authority in such a way as to enable comparison with the annual budget and council tax set for the year. The new statement would be prepared in addition to the statutory accounts, and would be subject to audit. An illustration of the new statement is provided at Annex 4 to the report.

Proposal for new service statement

42. The report consequently recommends that CIPFA/LASAAC should review the statutory annual accounts to determine whether there is scope to remove disclosures that may no longer be considered to be necessary.

43. Annex 5 of the report lists relevant recommendations made by the Kingman Review, CMA Study and Brydon Review, and comments on how Redmond has addressed them and how they may impact on the future of local authority audit.

Grant claims and other returns

Housing benefits certification

44. The Department for Work and Pensions (DWP) has issued the Module 5 Software Diagnostic Tool* component of the HBAP approach to the certification of the 2019/20 housing benefit subsidy claims for councils using Northgate Orbis benefit systems.

Submission of certified claims

45. The Scottish Government and the DWP have advised Professional Support that email submissions for grant claims (return and covering letter with electronic signatures) are acceptable and should be sent to the addresses listed in the following table:

Claim	Email address
Education Maintenance Allowances	Fraser.Young@gov.scot
Housing Benefit Subsidy	lawelfare.lapaymentsandsubsidy@dwp.gsi.gov.uk
Non-Domestic Rate Income	lgfstats@gov.scot

46. Paper copies should also be sent for the Scottish Government claims once their offices are open.

Advice to auditors

47. The following table summarises a selection of requests for technical advice made by auditors to Professional Support during the quarter in respect of the audit of the 2019/20 annual accounts of local government bodies, along with the advice offered:

Auditor Action
Auditors should consider the application of this advice to their own audits

Property, plant and equipment

Can a local government body capitalise a number of laptops that individually fall below the capitalisation de minimis?
Local government bodies can set a de minimis level for capital expenditure below which items will not be capitalised. Paragraph 4.1.4.1 of the accounting code requires the de minimis level to be disclosed in the accounting policies. A body could group similar items, such as laptops, and capitalise them even if individually they are below the de minimis. Where a body intends to group assets, they should explain that within their accounting policies.

Employee benefits/pension funds

What is the potential impact for the pension fund and for participating employers if a valuer discloses a material uncertainty in their valuation reports for investment property held by the pension fund at 31 March 2020?
The consideration for pension funds is the same in principle as when the valuer of local government bodies declares a material uncertainty in a valuation report for land and buildings (explained in Technical Bulletin 2020/2 at paragraph 14). An explanation should be added to the estimation uncertainty note. For participating bodies, the value of their attributable assets is estimated by rolling forward the valuation from the last triennial valuation at 31 March 2017. A material uncertainty declared in respect of the 31 March 2020 valuation does not therefore directly impact on the participating bodies' assets at that date. It could therefore be argued that the estimation uncertainty note is not required to highlight the material uncertainty. However, employer bodies should consider whether it may be helpful to users if they included a reference to the material uncertainty, for example, in the Management Commentary.

Arms length external organisations

A council has issued a letter of comfort to support an arms-length external organisation (ALEO) meet any liabilities that they are unable meet as a result of COVID-19. How should this be reflected in the council's financial statements?

The letter of comfort may constitute a financial guarantee if it requires the council to make specified payments to reimburse the holder of a debt if the ALEO fails to make a payment under a contract. Where this is the case, the accounting code requires the council to recognise the financial guarantee as a provision under IFRS 9. The provision should be recognised at fair value, estimated by considering the probability of the guarantee being called and the likely amount payable.

If the letter of comfort does not constitute a financial guarantee, it is likely that the disclosure by the council of a contingent liability would be appropriate.

The auditors of an ALEO have reported that the going concern basis of accounting is not appropriate. What impact does that have on the financial statements of the council?

It is likely that this is a sufficiently significant event after the year end to warrant disclosure in the council's annual accounts. The extent and nature of disclosure will be determined by the significance of the ALEO to the council's operations. Where the ALEO is to be disbanded, the arrangements for the continued delivery of its activities will be of interest to users.

Where the ALEO is included in the group financial statements as a subsidiary, further consideration will be required. The ALEO not being a going concern does not necessarily impact on the values of its assets and liabilities. For example, there may be an agreement that the assets and liabilities will transfer to the council at the carrying amount. Where that is not the case, and the ALEO's assets are considered to be overstated, and the overstatement is material to the group financial statements, a consolidation adjustment would be appropriate to remove the overstatement.

The auditors of the ALEO have reported that the going concern basis of accounting is not appropriate for the ALEO. What impact does that have on the Independent Auditors Report for the council?

The reporting by the council's auditor of conclusions related to going concern under ISA (UK) 570 relates only to the council itself. Going concern issues in respect of an ALEO do not affect those conclusions and therefore should not be reported in the 'conclusions related to going concern' paragraph in the Independent Auditor's Report.

Where the matter is considered to be of such importance that it is fundamental to users' understanding of the financial statements, an emphasis of matter paragraph should be considered under ISA (UK) 706. This may be the case where the ALEO is to be disbanded, and the arrangements for the continued delivery of its activities will have a substantial impact on the council.

Where the ALEO is included in the group financial statements as a subsidiary, and the ALEO's assets are considered to be overstated, and the overstatement is material to the group financial statements, auditors should consider whether a qualified opinion is appropriate if the material misstatement is not corrected.

Standards issued not yet adopted disclosure

What standards should local government bodies include in the 'standards issued but not adopted' disclosure in 2019/20

The accounting code requires a body to disclose information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted. This requirement is based on IAS 8 but applies only to accounting standards that come into effect for financial years commencing on or before 1 January of the financial year in question (i.e. on or before 1 January 2020 for 2019/20).

What standards should local government bodies include in the 'standards issued but not adopted' disclosure in 2019/20

The applicable standards to be disclosed in 2019/20 are set out in the subsequent edition of the accounting code (i.e. the 2020/21 accounting code). They are summarised in the following table:

Standard	Amendment	Potential impact
IAS 28 Investments in Associates and Joint Ventures: Long-term Interests in Associates and Joint Ventures	Applies to cases when an investment in an associate or joint venture is held by a third party (e.g. unit trust)	Unlikely to apply in practice to most local government bodies
IFRS 3 Business Combinations and IFRS 11 Joint Arrangements	Applies to cases where the body is a party to a joint arrangement and obtains control	Unlikely to apply in practice to many bodies
IAS 12 Income Taxes	Relates to the recognition of the income tax consequences of dividends	May impact on the group financial statements but Is not expected to be common
IAS 23 Borrowing Costs	Affects the specification for calculating borrowing costs which can be capitalised when a weighted average borrowing cost is used	May impact for any body with a policy of capitalising borrowing costs
Amendments to IAS 19 Employee Benefits: Plan Amendment, Curtailment or Settlement	Applies where a pension scheme amendment, curtailment or settlement occurs during the year. The amended assumptions, as used for the remeasurement of the net defined benefit liability, are to be applied in relation to the benefits for the remainder of the year	Impact if a pension scheme amendment, curtailment or settlement occurs during the year
Amendments to References to the Conceptual Framework in IFRS Standards	Updates references to the framework in certain accounting standards so they refer to the 2018 version rather than the 2010 one	May impact when bodies use the Conceptual Framework to develop and apply accounting policies when the accounting code or a standard does not apply to a transaction
Amendment to line item specifications for the net assets statement as detailed in paragraph 6.5.3.6 b) of the accounting code	Requires pooled investment vehicles to be analysed between equities, bonds, property, hedge funds, diversified growth funds, private equity funds, infrastructure funds and other	Impacts on pension funds

Bodies are required to disclose known or reasonably estimable information relevant to assessing the possible impact that application of the new standard will have on the body's financial statements in 2020/21.

As the implementation of IFRS 16 in the public sector has been delayed so that it will come into effect on 1 January 2021, the disclosure requirement in the accounting code does not apply to IFRS 16 in 2019/20 and no information requires to be disclosed.

Annual Governance Statement

How should a body report its compliance with the CIPFA statement on the Role of the Chief Finance Officer in Local Government?
The statement on the Role of the Chief Finance Officer in Local Government (CFO statement) codifies the role and responsibilities of the proper officer under Section 95 of the Local Government (Scotland) Act 1973. It applies on a 'comply or explain basis'. Bodies are required to prepare their Annual Governance Statement in accordance with the Delivering Good Governance in Local Government Framework. A key element of the governance arrangements set out in the framework is ensuring that financial management arrangements conform with the governance requirements of the CFO statement. Where the arrangements do not comply, paragraph 7.9 requires the body to explain in the Annual Governance Statement why that is the case and how they deliver the same impact.

Summary of auditor actions in this section

Paragraphs	Auditor actions
27 to 31	Evaluate whether bodies are considering the impact of the proposed McCloud remedy on pension liabilities
32 to 34	Evaluate whether bodies are considering the impact of the Goodwin Tribunal on pension liabilities
47	Consider the application of the advice from Professional Support to own audits

Contact points for this section

48. The contact points for this section of the Technical Bulletin are:

- Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk
- Anne Cairns, Manager (Professional Support) – acairns@audit-scotland.gov.uk (grant claims items only).

Section 3
Central government sector

Advice to auditors

49. The following table summarises a request for technical advice made by auditors to Professional Support during the quarter in respect of the audit of the 2019/20 annual report and accounts of central government bodies, along with the advice offered:

Auditor action
Auditors should consider the application of this advice to their own audits

Property, plant and equipment

Can a central government body capitalise a number of laptops that individually fall below the capitalisation threshold?
Central government bodies can choose whether to have a capitalisation threshold and, if so, set their own limits. Auditors should evaluate whether the body's threshold is appropriate to its circumstances and disclosed in the accounting policies. A body could group similar items, such as laptops, and capitalise them even if individually they are below the threshold. Where a body intends to group assets below the threshold, they should explain this within their accounting policies. Bodies may wish to consider the practicality of managing grouped assets within their asset register before implementing such a policy.

Summary of auditor actions in this section

Paragraphs	Auditor actions
49	Consider the application of the advice from Professional Support to own audits

Contact point for this section

50. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 4

Health sector

Advice to auditors

51. The following table summarises a request for technical advice made by auditors to Professional Support during the quarter in respect of the audit of the 2019/20 annual report and accounts of health boards, along with the advice offered:

Auditor action
Auditors should consider the application of this advice to their own audits

Property, plant and equipment

Can a health board capitalise a number of laptops that individually fall below the capitalisation threshold?
In contrast with central government bodies which can choose whether to have a capitalisation threshold and set their own limits, the Capital Accounting Manual (CAM) sets a threshold of £5,000. The CAM allows grouped items to be capitalised below that level subject to specified conditions. For example, they should be functionally interdependent, acquired at about the same date and have a similar useful life.

Summary of auditor actions in this section

Paragraphs	Auditor actions
51	Consider the application of the advice from Professional Support to own audits

Contact point for this section

52. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 5

College sector

Auditing developments

Technical guidance note on risks of misstatement in 2019/20

53. Professional Support has published Module 14 of Technical Guidance Note (TGN) 2020/1 to provide auditors with guidance on planning and performing the audit of 2019/20 annual report accounts of colleges.

54. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement in 2019/20. The TGN supplements the Code of Audit Practice and auditors are expected to pay it due regard and use it as a primary reference source when performing 2019/20 audits.

Auditor action
Auditors should pay due regard to Module 14 of TGN 2020/1

55. The structure of TGN 2020/1 comprises a number of modules:

- The Overview Module provides an overall introduction and covers risks of misstatement in areas that are pervasive to the financial statements as a whole.
- Modules 1 to 8 set out risks of misstatement for specific classes of transactions, balances and disclosures in the financial statements. These modules explain the appropriate related accounting treatment and set out the action auditors should undertake to evaluate whether the body has followed the required treatment.
- Module 9 covers irregularities in income and expenditure
- Module 10 covers the audited part of the Remuneration and Staff Report
- Module 11 sets out procedures for Statutory Other Information (i.e. Performance Report and Governance Statement).

56. Module 14 has been published to provide:

- guidance on applying the other modules to the audit of the annual report and accounts of colleges
- supplementary guidance on the risks of misstatements in the areas specific to colleges.

2019/20 model independent auditor's reports

57. Professional Support has published Technical Guidance Note 2020/6(C) 2019/20 Independent Auditor's Report for Colleges to provide auditors with the model Independent Auditor's Reports which should be used for the 2019/20 annual report and accounts.

58. The model Independent Auditor's Reports set out in the Appendices of the TGN have been tailored to reflect college legislation and augmented by the reporting requirements of the Auditor General. There have been no significant changes to the model Independent Auditor's Reports for 2019/20.

59. The TGN also provides guidance on the amendments that require to, or may, be made to the wording in the models in the form of auditor actions. Some enhancements have been made to the guidance to make the required auditor actions clearer. Auditors should complete for each report the checklist at Appendix 3 which provides a list of those auditor actions.

60. Any proposed modifications to any audit opinion or conclusion, or the inclusion of 'emphasis of matter' or 'other matter' paragraphs, should be discussed with Professional Support in advance of finalising the report.

Auditor action
Auditors should pay due regard to TGN 2020/6(C) when reporting 2019/20 audits

Annual report and accounts overall developments

2019/20 Accounts Direction

61. The Scottish Funding Council (SFC) has issued their Accounts Direction for Scotland's Colleges 2019/20. The direction requires colleges to:

- comply with the Statement of Recommended Practice: Accounting for Further and Higher education (SORP) in preparing their financial statements. The 2019 edition of the SORP applies in 2019/20
- include a Performance Report and Accountability Report in their annual report and accounts in accordance with the Government Financial Reporting Manual (FReM).

62. Specific mandatory disclosure requirements for colleges are set out in Appendix 2 to the direction. The main changes in Appendix 2 result from the impact of COVID-19 and those affecting the Performance Report are summarised in the following table:

Performance Report should reflect COVID-19

Area	Change
Adjusted Operating Position	The impact of COVID-19 should not be included as a separate adjustment to the Adjusted Operating Position. Where the impact on results is significant, the narrative in the Performance Report should provide an adequate explanation.
Performance analysis	Paragraphs 4 to 6 have been added to refer to the Addendum to the 2019/20 FReM (see Technical Bulletin 2020/2 – paragraph 60) which permits colleges to omit the performance analysis section from the Performance Report. Where relevant performance information has already been published elsewhere, colleges are encouraged to refer to the relevant publication.
Performance overview in Performance Report	Paragraph 7 sets out the minimum requirements for the performance overview. Where relevant, disclosures should explain the impact of COVID-19 and EU withdrawal, as well as any mitigating actions implemented by the college.

63. In addition, paragraph 28 requires the governance statement to explain any changes to the governance arrangements of the college, resulting from COVID-19.

Financial statements developments

Guidance on 2019/20 financial statements

64. The SFC has issued guidance notes on completion of the 2019/20 financial statements which are designed to supplement the accounts direction. The guidance covers key disclosures in the financial statements, including model disclosure notes set out at Annexes A to F.

65. The main change is that references included in previous years to guidance on an appropriate discount factor (net interest rate) as at 31 July and the spreadsheet for the calculation of the enhanced pension provision have been removed. Professional support understand that the SFC will not provide such guidance and colleges are expected to identify the appropriate discount factor.

Summary of auditor actions in this section

Paragraphs	Auditor actions
53 - 56	Pay due regard to Module 14 of TGN 2020/1 when planning and performing 2019/20 audits
57 - 60	Pay due regard to TGN 2020/6(C) when reporting 2019/20 audits

Contact point for this section

66. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 6
Professional Matters

Revised auditing standard on risks of material misstatement

Significant judgements require to be disclosed

67. The Financial Reporting Council (FRC) has a issued a revised ISA(UK)315 Identifying and Assessing the Risks of Material Misstatement as a result of recent revisions to the international standard.

68. The effective date of the revised standard is for accounting periods beginning after 15 December 2021.

69. The main revisions are summarised in the following table:

Area	Summary of revision
IT business environment	This includes requiring the auditor to understand the entity's use of IT in its business, the related risks and the system of internal control addressing such risks.
Automated audit tools and techniques	Additional application guidance on the use of automated tools and techniques by auditors.
Enhancing professional scepticism	An emphasis has been added on the need for auditors to not bias their work toward obtaining corroborative evidence or excluding evidence that is contradictory. A new requirement for the auditor, towards the end of the risk assessment process, to consider all audit evidence obtained from performing risk assessment procedures, whether corroborative or contradictory.
Purpose of risk assessment	Clarification has been added that the purpose of performing risk assessment procedures is to obtain audit evidence that provides an appropriate basis for the identification and assessment of the risks of material misstatement and the design of further audit procedures
Inherent risk factors	The concept of 'inherent risk factors' has been introduced to assist the auditor in identifying events or conditions that may affect the susceptibility of assertions about classes of transactions, account balances or disclosures to misstatement.
Significant class of transactions, account balances or disclosures	This new concept refers to those classes for which there are assertions with an identified risk of material misstatement (referred to as relevant assertions).
Spectrum of inherent risk	This new concept applies to the extent to which inherent risk varies
Significant risk	This relates to an identified risk of material misstatement for which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur.
Control risk	Guidance has been added explaining that, if the auditor does not plan to test the operating effectiveness of controls, control risk should be assessed as the same as the assessment of inherent risk.

Thematic review of COVID-19 financial reporting effects

70. The FRC has issued a report that summarises the key findings of their review of the financial reporting effects of COVID-19 for a sample of annual accounts ending 31 March 2020.

71. The report is intended to provide useful guidance for entities by identifying areas where disclosures affected by COVID-19 can be improved, as well as providing examples demonstrating the level of detail provided by better disclosures. The following table summarises the key messages for selected areas:

Area	Report pages	Key messages
Strategic report (the private sector equivalent of the Management Commentary/ Performance Report).	22 to 31	• The forward-looking information provided in the Strategic Report is particularly important as that is where users of accounts focus to enable them to understand how an entity intends to navigate through COVID-19 related challenges. • It is important to explain clearly how the future strategy and business model may be affected by COVID-19. • Entities are expected to consider the specific resources, assets and relationships that are most under threat and the steps being taken to protect them when setting out their principal risks and uncertainties. • All stakeholders are concerned not only about an entity's workforce and how they are being retained and supported but also about how supplier, customer and other relationships have been maintained.
Presentation of the financial statements	33 to 34	• Entities need to consider whether additional items of income and expenditure arising from the COVID-19 pandemic should be separately disclosed in accordance with their existing policies for 'exceptional' items. It is good practice to include all such items in a single note or link them with cross references. • Where the effects of COVID-19 are pervasive and hard to quantify, it is helpful to provide narrative disclosures explaining the nature of the items and the uncertainties around them. • Entities are discouraged from splitting discrete items on an arbitrary basis in an attempt to quantify the portion relating to COVID-19 as it is unlikely to provide users with reliable information.
Disclosure of significant judgements and estimates	39 - 41	• Where entities find it difficult to estimate which uncertainties will crystallise or which assumptions will change within 12 months, they should consider whether a longer period is more relevant in explaining certain risks, and should tailor their disclosures to their specific circumstances. • The disclosure of sensitivity analysis or information about the range of possible outcomes in relation to estimation uncertainty is particularly valuable to users. The review identified a high number of instances where such disclosures were incomplete or missing altogether.
Impairment of non-financial assets	44 to 47	• Entities are expected to consider the pandemic an indicator of impairment because of the adverse effect it has had. • Most companies identified the impairment assessment as a key source of estimation uncertainty, and explained that the value-in-use method for calculating the recoverable amount of assets requires management to determine appropriate assumption.

Area	Report pages	Key messages
Events after the reporting period	51	• The assessment of whether there are any adjusting post balance sheets events must be made without the benefit of hindsight to ensure assets and liabilities reflect the conditions as at the period end. • As the pandemic is made up of a series of events, it may be difficult to determine whether a post balance sheet event is an adjusting or a non-adjusting event. Disclosures are required in cases where management has exercised significant judgement in making this determination. • Entities should follow the guidance in IAS 37 to determine whether a post balance sheet event is adjusting or non adjusting in cases where IAS 37 covers the specific event or circumstance, e.g. redundancy provisions.

Technical Bulletin 2020/3

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Technical Bulletin 2020/4

Technical developments and emerging risks from October to December 2020

Prepared for appointed auditors and audited bodies in all sectors

16 December 2020

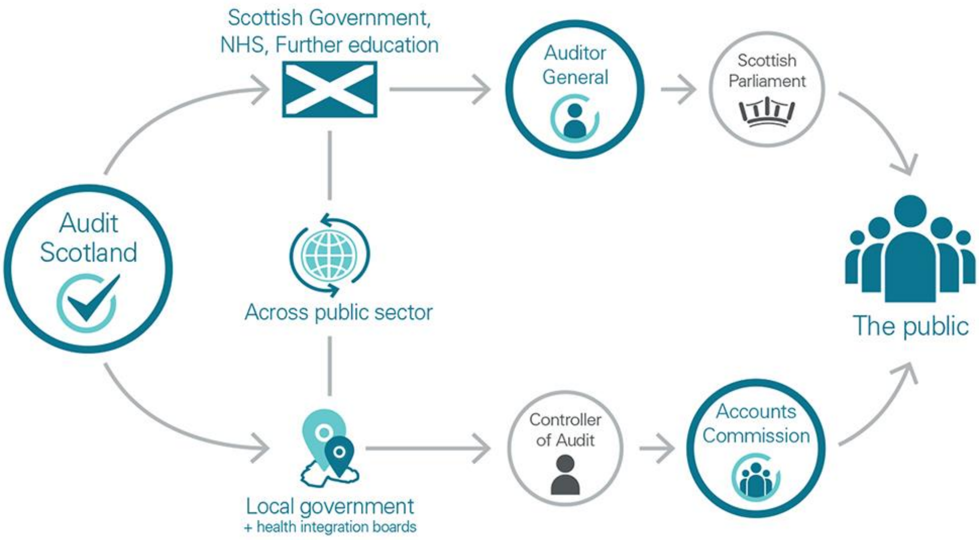
Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.

- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.

- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money

- reporting our findings and conclusions in public

- identifying risks, making clear and relevant recommendations.

Contents

Introduction

Purpose

> Technical Bulletins provide information on developments and guidance on emerging risks

1. The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- guidance on any emerging risks identified in the quarter.

2. Appointed auditors are required to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require to be aware of. It may still be necessary for auditors to read the source material if greater detail is required. These can be accessed by using the hyperlinks. They are also available from the Technical Reference Library maintained by Professional Support.

3. The actions by auditors recommended by Professional Support in respect of each item are highlighted in red and are also summarised at the end of each section.

4. Technical Bulletins are also published on the Audit Scotland website and therefore are available to audited bodies and other stakeholders. However, hyperlinks in this bulletin indicated with an asterisk link to documents on the Technical Reference Library and therefore are active only for auditors.

Highlights summary

5. Professional Support draws attention in the following table to certain items in this Technical Bulletin:

Highlights summary		
Professional Support has published guidance on planning 2020/21 audits [see paragraph 7]	PAF has issued a revised edition of PN 10 [see paragraph 11]	Professional Support has published guidance on risks of misstatement in 2020/21 local government annual accounts [see paragraph 22]
CIPFA has issued guidance notes on the 2020/21 accounting code [see paragraph 26]	CIPFA/LASAAC has issued a consultation on applying IFRS 16 to housing tenancies [see paragraph 30]	LASAAC has issued draft revised guidance on reserves for consultation [see paragraph 33]
The Scottish Government has announced financial flexibilities for councils [see paragraph 35]	The Scottish Government has announced further COVID-19 support schemes [see paragraph 41]	CIPFA/LASAAC and Treasury have deferred implementing IFRS 16 until 2022/23 [see paragraphs 30 and 62]
The FRC has issued proposed revisions to the audit standard on fraud [see paragraph 66]	The FRC has issued a report on developments in audit [see paragraph 69]	The FRC has issued a report on corporate reporting [see paragraph 86]

Contact point

> Feedback on this Technical Bulletin is welcome

6. The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – pobrien@audit-scotland.gov.uk.

Section 1
Cross-sector

Guidance on planning 2020/21 audits

7. Professional Support has issued guidance to assist all appointed auditors in planning their 2020/21 audits of public bodies. The guidance is available to auditors with other supporting materials on SharePoint* but is also freely available on the Audit Scotland website.

8. The guidance covers the main activities that comprise core audit work and the products associated with each activity. It recognises the impact of COVID-19 on the timing of the 2019/20 audits and the consequent late start to 2020/21 audits, the challenges in completing audits remotely, and the additional complexities and uncertainties.

9. The following table provides a summary of the key changes from last year, along with the section of the guidance in which further information is provided:

Nature of change	Relevant section
Submission deadlines for Annual Audit Plans have been moved back a month	1
Rates for additional audit work have been revised	1
Submission deadlines for audited annual accounts have been provisionally moved	2
Guidance has been provided to focus auditors' risk assessments on the audit dimensions in light of the impact of COVID-19	3A
Reporting on the risk of fraud and corruption in the procurement function may be in 2020/21 or 2021/22 Annual Audit Reports	3A
Submission deadline for Best Value Audit Plans have been moved back to 30 April	3B
The list of councils where a Best Value Assurance Report is required has been updated	3B
Guidance added clarifying Best Value work in other local government bodies	3B
Auditors in local government are not required to consider Strategic Audit Priorities	3C
Guidance updated on considering the arrangements for statutory performance information in local government	3D
No requirement for auditors to contribute to performance audit reports or impact reports	4
Guidance updated on involvement in National Fraud Initiative	5K

10. The guidance supplements the Code of Audit Practice, and auditors are therefore required to plan their 2020/21 audits in accordance with it.

Auditor action
Auditors should plan their 2020/21 audits in accordance with this guidance

Revised practice note on auditing public bodies

Auditor action
Auditors should pay due regard to PN 10

11. The Public Audit Forum has issued a revised version of Practice Note 10 Audit of Financial Statements and Regularity of Public Sector Bodies in the UK (PN 10). Audit Scotland and the other UK audit agencies require auditors to pay due regard to PN 10. It comprises the following two parts:

- Part 1 contains guidance on the application of quality control and auditing standards to the audit of public sector bodies. It is based on standards which were in effect at 1 September 2020. Paragraph 1-1 indicates the standards on which application guidance is provided.
- Part 2 sets out guidance on the audit of, and expressing an opinion on, the regularity of transactions.

12. A significant aspect of PN 10 is the guidance on applying ISA (UK) 570 Going Concern to the public sector. Paragraphs 1-147 to 1-183 of PN 10 have been extensively revised to clarify the importance of the applicable financial reporting framework in determining the extent of the auditor's procedures.

Guidance on going concern has been refreshed

13. If the financial reporting framework requires the adoption of the going concern basis of accounting due to the anticipated continuation of service provision, auditors apply paragraphs 1-157 to 1-164. In essence, the going concern basis of accounting will continue to be appropriate at least until there is an intention to wind up the body.

14. Where there is a known intention to wind up a body, paragraphs 1-167 to 1-176 apply. Where the body's activities are likely to be transferred elsewhere in the public sector, the going concern basis of accounting is likely to remain appropriate. If the activities are not to be transferred within the public sector, auditors may decide to request that the body secures from the relevant department a letter of support.

15. A summary of the other main changes to PN 10 is provided in the following table:

ISA (UK)	Key changes
540	The issue in December 2019 of the revised standard on auditing estimates has been reflected. Guidance has been added at paragraph 1-116 on inherent risk factors relevant to the public sector, with examples such as • a very high degree of estimation uncertainty caused by the need to project forecasts far into the future, such as liabilities relating to defined benefit pension schemes • areas where there may be a lack of available comparators for estimates that are unique to the public sector, such as the valuation of important public assets • the existence of possible constructive obligations created by political statements or past practice of carrying out actions that may be expected of public authorities but are not required by law • general political uncertainty and the possibility of future changes in public policy having an impact on the assumptions used to prepare accounting estimates.
560	The guidance on determining the date the financial statements are authorised for issue and the date they are issued has been refreshed. Paragraph 1-136 has been amended to advise that central government financial statements are considered to be issued on the date of laying rather than the date of despatch for laying.
720	Paragraph 1-226 has been added to provide guidance on when the reporting framework requires that the 'other information' presented is fair, balanced and understandable. Paragraph 1-228 has been added on statutory other information, on which the auditor is required to express a positive statement in the auditor's report.

Guidance for auditors on 2019/20 Whole of Government Accounts

16. Professional Support has published Technical Guidance Note 2020/7 to provide auditors with guidance on examining and reporting on the 2019/20 Whole of Government Accounts (WGA) returns of relevant public bodies. The TGN is available with supporting material to auditors on SharePoint and is also freely available from the Audit Scotland website.

17. The National Audit Office (NAO) is the group auditor for WGA and has prescribed a threshold for auditor assurance of £500 million for 2019/20 for all public bodies in Scotland. No examination is required for bodies below the threshold but auditors are required to partially complete the Assurance Statement and submit it to the NAO. Testing and other procedures that auditors are required to undertake in respect of providing assurance to the NAO on 2019/20 WGA returns above the threshold are set out in the TGN.

18. The main changes from 2018/19 are as follows:

- Data will be collected for the 2019/20 WGA by bodies inputting information directly to the Online System for Central Accounting and Reporting.
- Bodies will be able to run the counterparty matches report (now called the Matches Analysis Tool) themselves.
- Gateway tests are no longer required. The validation test, that was previously a gateway test, is now conducted as a fieldwork test.
- Auditors are required to submit an Audit Completion Template and the final WGA return to Treasury.

Auditor action

Auditors should examine the 2019/20 WGA returns in accordance with this guidance

19. Auditors are required to examine and report on 2019/20 WGA returns in accordance with this TGN.

Summary of auditor actions in this section

Paragraphs	Auditor actions
7 - 10	Plan 2020/21 audits in accordance with the guidance on planning
11 - 15	Pay due regard to the revised PN10 in applying auditing standards to the audit of public bodies
16 – 19	Examine and report on 2019/20 WGA returns in accordance with TGN 2020/7

Contact point for this section

20. The contact for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Section 2

Local government sector

Auditing developments

Technical Guidance Note on risks of misstatement in 2020/21

22. Professional Support has published Technical Guidance Note (TGN) 2020/8(LG) to provide auditors with guidance on risks of misstatement in 2020/21 annual accounts of local government bodies. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

Auditor action
Auditors should pay due regard to TGN 2020/8(LG)

23. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement in 2020/21. The TGN supplements the Code of Audit Practice and auditors are expected to pay it due regard and use it as a primary reference source when performing 2020/21 audits.

24. The TGN structure comprises a number of modules as summarised in the following table:

Module	Risks of misstatement area	Purpose
Overview	Areas that are pervasive to the financial statements as a whole	Explains the appropriate related accounting treatment and sets out the action auditors should undertake to evaluate whether the body has followed the required treatment
1 - 9	Specific classes of transactions, balances and disclosures in the financial statements.	
10	Audited part of the Remuneration Report	Explains the requirements and sets out the action auditors should undertake
11	Statutory Other Information (e.g. Management Commentary and Annual Governance Statement)	Sets out the procedures for considering the Statutory Other Information
12	Integration joint boards	Provides guidance on the application of the above modules to these specific bodies
13	Pension fund accounts	
14	Section 106 charities	

25. The risks of misstatement for 2020/21 have been updated to reflect new requirements and risks which emerged during the 2019/20 audits that remain applicable.

Financial statements developments

2020/21 guidance notes

26. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued guidance notes* on the 2020/21 accounting code*. The overall aim of the guidance notes is to explain and illustrate how to apply the accounting requirements of the accounting code, provide background to those requirements, and illustrate how they might be applied in practical situations. The guidance is not mandatory.

The guidance notes are not mandatory

27. This edition of the guidance notes has been updated to reflect changes to the 2020/21 accounting code including the following:

- Amendments to reflect changes to the definition of material which now makes reference to the concept of obscuring information.
- Implementation of amendments to IAS 19 in respect of a pension scheme amendment, curtailment or settlement occurring during the year.
- Amendments to the disclosure requirements for pension funds in respect of pooled investment vehicles.
- Clarifications in respect of aspects of financial instruments.

The guidance notes have been updated to reflect changes to the 2020/21 accounting code

Proposed change to accounts deadlines for 2020/21

28. The Scottish Government is consulting* on proposed changes to the approval and publication deadlines for the 2020/21 annual accounts. The proposed changes are set out in the following table:

Action	Current date	Proposed date
Approval to sign off accounts	30 September	31 October
Publication of accounts	31 October	15 November

29. There are no proposed changes to the 30 June deadline for the unaudited accounts.

Consultation on secure tenancies under IFRS 16

30. The CIPFA/LASAAC Local Authority Code Board (CIPFA/LASAAC) will shortly be issuing for consultation proposals on how housing secure tenancy agreements should be treated under IFRS 16 Leases. CIPFA/LASAAC has announced the further deferral of the implementation of IFRS 16 until 1 April 2022. The proposals in the consultation are therefore expected to affect the 2022/23 accounting code.

31. The consultation questions, with additional information, are summarised in the following table:

Question	Consideration and proposal
Is a secure tenancy agreement a lease for accounting purposes?	On the balance of factors, the proposal is that secure tenancy agreements meet the definition of a lease in IFRS 16.
Is it a finance or an operating lease?	Based on a consideration of both primary and secondary indicators, secure housing tenancy agreements are operating leases. There is a proposal to include an interpretation in the accounting code so that housing tenancy agreements are classified as operating leases.
What disclosures are requirement?	Disclosure requirements for operating leases are either already met by existing disclosures or are not relevant. There is a proposal to include an interpretation that operating lease disclosure requirements do not apply.

32. Comments on the proposals should be sent to cipfalasac@cipfa.org.

Consultation on revised reserves guidance

33. The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) has issued a consultation paper of updated guidance on the statutory basis and accounting for reserves. The guidance issued in 2005 is being revised for changes in the financial reporting framework in the period since then. It is also proposed that the status of the guidance should be changed to mandatory.

34. Comments should be sent to lasaac@cipfa.org by 29 January 2021. They are particularly requested on the aspects of the guidance set out in the following table:

Aspect	Paragraph	Nature of change
The recommended distinction between mandatory and discretionary earmarking	20	It is recommended that local government bodies draw a distinction between: • 'mandatory earmarked balances', e.g. gains on financial assets classified as fair value through profit or loss; and • 'voluntary earmarked balances', e.g. reflecting the body's discretionary financial management plans for the use of funds.
The new requirement to separately disclose any deferred capital receipts	30	Deferred capital receipts include sales proceeds paid in instalments. Where deferred capital receipts are held in the Capital Fund, it is proposed that the relevant balance should be specifically disclosed in the notes.
The guidance on the treatment of capital expenditure funded from the Renewal and Repair Fund	32	An amount equivalent to the capital expenditure incurred should be transferred from the Renewal and Repair Fund to the Capital Adjustment Account.
The specified treatment for the valuation element of depreciation	50	The accounting code allows local government bodies to either: • treat all depreciation as a statutory adjustment; or • split depreciation into the historical cost element (statutory adjustment to Capital Adjustment Account) and the valuation element (reserve transfer to Revaluation Reserve). For consistency of reporting, the guidance proposes making the second option mandatory. The option treating the valuation element of depreciation as a statutory adjustment would therefore be withdrawn.
The requirement to disclose earmarked elements of the General Fund	54	The accounting code requires an analysis of earmarked reserves to be disclosed in a note. The guidance proposes applying that requirement to earmarked elements of the General Fund or other statutory fund.

Financial flexibilities for 2020/21 and 2021/22

35. A package of financial flexibilities has been agreed between the Scottish Government and the Convention of Scottish Local Authorities to address the funding pressures faced by local government due to COVID-19.

36. The flexibilities will be available in 2020/21 and/or 2021/22, and are summarised in the following table:

Area	Years	Nature of flexibility
Application of capital receipts	2020/21 and 2021/22	Councils will be permitted to use capital receipts to finance the financial impact of COVID-19.
Revision of statutory charge for leases and service concession arrangements	Apply from 2020/21 or 2021/22	Councils will be allowed to charge depreciation to the General Fund over the life of the asset rather than charge the debt element over the contract period. Councils will have the flexibility to apply this change in either 2020/21 or 2021/22 and this approach will apply to all such arrangements from the implementation of IFRS 16 Leases.

Area	Years	Nature of flexibility
Loans fund repayment holiday	2020/21 or 2021/22	Councils will be permitted to defer loans fund repayments due to be repaid in either 2020/21 or 2021/22.

37. The Scottish Government expects councils to consider:

- the contribution their reserve balances can make to meeting their funding pressures
- the resources available from capital receipts and the change in accounting arrangements for leases and service concession arrangements before taking advantage of a loans fund repayment holiday.

Capital receipts

38. Draft statutory guidance* has been issued in respect of the use of capital receipts. Key aspects of the proposals are summarised in the following table:

Aspect	Proposal
Qualifying expenditure	The statutory guidance does not define qualifying expenditure. The local authority will be required to demonstrate, by reporting to full council, how the capital receipts are to be used to fund the financial impact of COVID-19. Full council will be required to approve the use.
Qualifying capital receipts	Only capital receipts received in 2020/21 or 2021/22 can be applied. The decision on use is required to be made in the year the capital receipt is recognised.
Accounting treatment	The capital receipt requires to be transferred as a statutory adjustment to the Capital Grant and Receipts Unapplied Account in the year of receipt. Capital receipts so transferred in 2020/21 can be applied in that year or in 2021/22. Any unused capital receipts at 21 March 2022 would be transferred to the Capital Fund.
Disclosure requirements	The reason for each transfer of capital receipts from the Capital Grants and Receipts Unapplied Account to the General Fund or Capital Fund should be disclosed. All the elements of the balance on the Capital Grants and Receipts Unapplied Account are to be disclosed separately.

39. Comments should be sent to Hazel.Black@gov.scot by 18 January 2021.

Loans fund repayment holiday

40. The Local Authority (Capital Finance and Accounting)(Scotland)(Coronavirus) Amendment Regulations 2021* are being prepared in respect of the loans fund repayment holiday. This will allow a council to defer loans fund repayments due in either 2020/21 or 2021/22 (but not both years). Any deferred repayment is to be repaid within the shorter of:

- the remaining period of the loans fund advance to which that deferral relates; or
- 20 years.

New COVID-19 support schemes

41. The Scottish Government has provided information on the following two new COVID-19 support schemes that are being administered by councils:

- Restrictions Fund
- Strategic Framework Business Fund.

42. The Restrictions Fund ran from 9 October until 1 November and was intended to support employees and businesses impacted by the COVID-19 restrictions that came into force in that period. The four individual funds comprising the Restrictions Fund are summarised in the following table:

Fund	Applicability	Rateable Value (RV)	Grant
Closure Fund	Business premises in the five health board areas that had to close	RV of up to and including £51,000	£2,875
		RV of £51,001 and above	£4,310
Furlough Costs Fund	Business premises in the five health boards that were required to close and furlough employees	N/A	£1,650
Hardship Fund	Business premises that remained open but were significantly impacted by the restrictions including those in the direct supply chains of firms that closed	RV of up to and including £51,000	£1,440
		RV of £51,001 and above	£2,155
Contingency Fund of £11 million	Businesses not covered by the above funds (night clubs and soft play)	RV of up to and including £18,000	£10,000
		RV of between £18,001 - £51,000	£25,000
		RV of above £51,001	£50,000

43. The Strategic Framework Business Fund is intended to support businesses required to close by law, or to significantly change their operations, due to COVID-19 restrictions from 2 November 2020. The two grants are summarised in the following table:

Grant	RV up to and including £51,000	RV more than £51,000
Temporary closure	£2,000	£3,000
Business restrictions grant (business is specifically required to modify its operations)	£1,400	£2,100

44. Grants will be paid every 4 weeks in arrears as long as restrictions last. Grant funding for eligible businesses will cover the period of any closures or restrictions with the earliest claim date being 2 November 2020.

Bulletin on McCloud and Goodwin cases

45. CIPFA issued a supplement to CIPFA Bulletin 5 to provide an update on the McCloud and Goodwin cases in respect of pension liabilities. It confirmed that the Scottish Government consultation on proposals to provide a remedy to the McCloud and Sargeant cases is an adjusting event.

46. Local government bodies were advised to assess whether the change in the assumptions would make a material difference to the estimate of pension liabilities. If the difference was material, bodies were advised to commission revised IAS 19 reports and adjust the 2019/20 accounts accordingly.

47. For the Goodwin case, although proposals have not yet been published, a statement from the Treasury confirmed that changes will be required that will increase pension liabilities. The bulletin advised bodies to consider, in discussion with their actuaries, the materiality of the impact on pension liabilities and therefore whether an adjustment is required in 2019/20.

Statutory Other Information developments

Guidance on internal audit assurance

48. CIPFA has issued guidance on the provision of internal audit assurances in 2020/21. The impact of COVID-19 has raised the question of whether internal audit will be able to undertake sufficient work during 2020/21 to fulfil the requirements of the Public Sector Internal Audit Standards (PSIAS). Specifically, the head of internal audit (HIA) is required to issue an annual opinion on the overall adequacy and effectiveness of the body's framework of governance, risk management and control.

49. The guidance confirms that the professional and regulatory expectations on local government bodies to ensure that their internal audit arrangements conform with PSIAS have not changed. HIAs need to consider whether they can still issue the annual opinion or whether there will need to be a limitation of scope. A limitation of scope arises where the HIA is unable to draw on sufficient assurance to issue a complete annual opinion in accordance with the professional standards.

HIAs need to consider a limitation of scope

50. This guidance addresses the importance of early identification of the risk of limitation of scope. It suggests the following mitigating actions to avoid such a limitation where possible:

- The HIA should plan to obtain sufficient assurance to support the annual opinion, taking into account both internal audit work and other sources of assurance. The reliance the HIA is placing on other sources of assurance should be disclosed in the overall opinion.
- The HIA, leadership team and audit committee should review and discuss internal audit capacity where there are concerns and develop an action plan to mitigate the risk.
- The HIA should make best use of their audit resources to maximise assurance.
- Where the HIA considers that a limitation of scope is likely, the leadership team and audit committee should be advised promptly. The HIA should set out the likely consequences assessed and advise on remedial action to avoid a limitation of scope.

51. If a limitation of scope does become necessary, page six of the guidance suggests possible wording for the HIA to use in the report depending on the type of limitation.

52. The HIA opinion is one of the sources of assurance that the body relies on for its annual governance statement. Where the HIA annual opinion contains a limitation of scope, the guidance advises the body to state this in the annual governance statement.

Grant claim certification

Housing subsidy certification

53. The Department for Work and Pensions (DWP) has revised the software diagnostic tool component (Module 5) of the approach to the certification of the 2019/20 housing benefit subsidy claims for councils using Capita benefit systems.

54. The Social Security (Scotland) Act 2018 (Information-Sharing and Scottish Child Payment) (Consequential Provision and Modifications) Order 2020 provides for the new Scottish Child Payment to be disregarded as income or capital when determining a claimant's entitlement to housing benefit.

Summary of auditor actions in this section

Paragraphs	Auditor actions
22 - 25	Pay due regard to TGN 2020/8(LG) when planning and performing the audit of the 2020/21 annual accounts

Contact point for this section

55. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk

Section 3

Central government sector

Financial statements developments

2020/21 discount rates

56. HM Treasury has issued PES(2020)12* which announces the change in the discount rate for general provisions, post-employment benefits liabilities, and financial instruments as at 31 March 2021.

57. The nominal discount rates to be applied as at 31 March 2021 for discounting general provisions recognised under IAS 37 are set out in the following table:

Category	Period	Percentage
Short term	Within 5 years	(0.02%)
Medium term	Between 5 and 10 years	0.18%
Long term	Between 10 and 40 years	1.99%
Very long term	More than 40 years	1.99%

Auditor action

Auditors should refer to this guidance when auditing the 2020/21 financial statements

58. As nominal rates do not take inflation into account, cash flows require to be inflated separately. There is a rebuttable assumption that the inflation rates specified in the paper will be used (unless other rates are clearly more applicable). The specified rates are:

- 1.2% for up to one year from the year end
- 1.6% between one and two years
- 2% for after two years.

59. The discount rates for post employment benefits are set out in the following table:

Use	Rate from 31 March 2021
Real rate used for valuing unfunded pension scheme liabilities and early departure provisions	(1.03)%
Nominal rate for unwinding discount on liabilities (interest)	1.25%
Rate used for funded pension schemes	Based on returns from AA corporate bonds at 31 March

60. The financial instrument discount rates to be applied at 31 March 2021 are set out in the following table:

Type	Rate
Real rate when financial instrument indexed to RPI	0.7%
Nominal rate when financial instrument is not linked to an inflationary index	3.7%

61. The paper also specifies a rate to be used for leases under IFRS 16. The 2021 nominal lease discount rate of 0.91% is only relevant for transition to IFRS 16 and for new leases that commence or are remeasured between 1 January 2021 and 31 December 2021.

IFRS 16 implementation

62. Treasury has issued a letter* announces the deferral of implementing IFRS 16 Leases until 1 April 2022. The delay is in light of pressures caused by the COVID-19 pandemic.

63. Bodies are permitted to implement IFRS 16 from 1 April 2021 provided they obtain approval from the Scottish Government.

Effective date for IFRS 16 will be 1 April 2022

Summary of auditor actions in this section

Paragraphs	Auditor actions
56 - 61	Refer to the guidance on 2020/21 discount rates

Contact point for this section

64. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 4
Professional matters

Auditing developments

Proposed revisions to standard on fraud

65. The Financial Reporting Council (FRC) has issued proposed revisions to ISA (UK) 240 The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements. Comments should be sent to AAT@frc.org.uk by 29 January 2021.

66. The proposed revisions are intended to:

- address the recommendation in the Brydon Review (covered in Technical Bulletin 2020/1 – paragraph 88) to clarify the obligations of auditors in respect of detecting fraud
- include enhancements of the requirements for the identification and assessment of risk of material misstatement due to fraud and the procedures to respond to those risks.

The proposals address the Bryden recommendation in respect of clarity over responsibilities

67. The main proposed revisions are summarised in the following tables:

Introduction

Paragraph	Proposal
3	Clarification that the evaluation of whether fraud is material should take into account the qualitative as well as quantitative characteristics of the fraud.
7-1	Clarification that the higher risk of not detecting a material misstatement resulting from fraud compared with error does not diminish the auditor's responsibility to obtain reasonable assurance about whether the financial statements are free of material misstatement due to fraud.

Professional scepticism

Paragraph	Proposal
12-1	New requirement that the auditor should not be biased towards obtaining evidence that may be corroborative or towards excluding audit evidence that may be contradictory.
13-1 and A9-1	Clarification that the auditor should remain alert for conditions that indicate a record or document may not be authentic. Examples are provided of conditions that may indicate a physical or electronic document is not authentic or has been tampered with.
14	New requirement for the auditor to investigate responses to inquiries that appear implausible.

Discussion among the audit team

Paragraph	Proposal
15-1 to 15-3 and A11	Specification of matters to be covered in the discussion, including how management could perpetrate and conceal fraudulent financial reporting and how assets of the entity could be misappropriated. Examples of matters that may be discussed are provided.

15-4	New requirement that the appointment lead should determine whether there should be further discussions at later stages in the audit to consider fraud risk factors. Examples of circumstances where it may be beneficial to have a further discussion are provided.

Risk assessments

Paragraph	Proposal
16	Clarification that the understanding obtained by the auditor includes the fraud risk factors relevant to the entity that affect the susceptibility of assertions to material misstatement due to fraud.
18-1	New requirement that the auditor makes inquiries of those persons who are responsible for dealing with allegations of fraud raised by employees or other parties.
21-1	Emphasis that the auditor should determine the implications for the audit if responses to inquiries of those charged with governance are inconsistent with the responses to the inquiries of management.
24-1, 27-1 and A27-1	New requirements that the auditor should determine whether the audit team requires specialised skills or knowledge to perform particular procedures and, whether a forensic expert is needed to investigate a fraud further. Examples of matters that may affect the auditor's determination are provided.

Responses to the assessed risks

Paragraph	Proposal
32-1	Emphasis that in evaluating possible management bias in making accounting estimates, the auditor should also comply with the relevant requirements in ISA (UK) 540.
36-1	Emphasis that in performing the overall evaluation of audit evidence, the auditor should evaluate whether: • the assessments of the risks of material misstatement at the assertion level due to fraud remain appropriate • sufficient appropriate audit evidence has been obtained regarding the assessed risks of material misstatement due to fraud, and should conclude whether the financial statements are materially misstated as a result of fraud.

Independent auditor's report

Paragraph	Proposal
39-1	Clarification that, when explaining the extent to which the audit was considered capable of detecting irregularities, including fraud, the wording should not be 'boilerplate'.

Communications to management and those charged with governance

Paragraph	Proposal
42	New requirement that the auditor should consider any matters regarding management's process for identifying and responding to the risks of fraud and the auditor's assessment of the risks of material misstatement due to fraud.

Communications to management and those charged with governance

Paragraph	Proposal
45-1	Emphasis that the auditor should document how they addressed any identified information that is inconsistent with their final conclusion regarding a significant matter.

Report on developments in audit during 2020

68. The FRC has issued its Developments in Audit report for the year. The report focuses on the work the FRC undertook to drive improvements in audit quality during 2020.

Inconsistent audit quality

69. The FRC's quality monitoring activities again showed that audit quality remained too inconsistent; 49 out of the 130 audits inspected in the 2019/20 inspection cycle required either improvement or significant improvement.

70. Insufficient challenge of the management of audited bodies remains one of the most frequent issues identified. The need to challenge management often arises when auditors evaluate their forward-looking judgements and estimates. Management may be consciously or unconsciously biased towards particular outcomes or assumptions.

Insufficient challenge of management

71. Auditors may also have an unconscious bias towards corroborating management's assumptions, rather than challenging them or seeking alternative evidence. They may also rely too much on prior knowledge, leading to a ready acceptance of management's assumptions.

72. The report highlights that establishing the extent of evidence needed to support a judgement in relation to uncertainties is a skill rather than a specific audit test. It requires the correct mindset and sufficient professional scepticism in evaluating the facts presented by management and how these compare to other evidence obtained. Auditors should form their own informed expectations as this would allow the auditor to identify and consider objectively the range of evidence relevant to the audit issue, and to ask the right questions, often through an iterative process requiring multiple discussions and time for reflection.

73. The report is clear that auditors need to understand why they continue to underperform in this area. Audit firms should encourage audit partners to take the time required when dealing with large and complex judgements. Where necessary, effective challenge of management should be given a higher priority than meeting deadlines.

Impact of COVID-19 on audit work

74. The inconsistent audit quality was found in audits that were completed before the impact of COVID-19. The economic impact of the pandemic has increased the complexity of many forward-looking accounting judgements. This makes effective challenge of management even more difficult.

75. The areas where the most significant impacts of the pandemic on auditing have been, and will continue to be, are summarised in the following table:

Area	Impact
Judgement	COVID-19 has made the business prospects of some companies highly uncertain, raising questions about whether there is a material uncertainty around going concern. Other judgements have also become more difficult, for example, valuation of illiquid or intangible assets and impairment assessments.
Remote working	The inability to meet with management face-to-face continues to create additional risks and complexities, particularly for areas where auditors normally obtain evidence in person, such as inventory counts.
Controls and fraud risk	Controls may be less effective, as some companies have cut back on the number of people involved in the internal control processes. For example, 45% of internal audit staff had been redeployed to support other areas of the business, while 15% were furloughed.

Accounting developments

IFRS adoption process

76. The FRC has issued a letter that explains the arrangements that will be in place for accounting and reporting standards after the UK leaves the EU.

77. All UK incorporated companies that are currently required to use international accounting standards that have been endorsed by the EU (EU-adopted IFRS) will need to use UK-adopted IFRS for financial years that begin on or after 1 January 2021.

IFRS will be endorsed by a UK board

78. Public sector bodies will use EU-adopted IFRS for 2020/21 and will move to UK-adopted IFRS in 2021/22.

79. On 1 January 2021, UK-adopted IFRS and EU-adopted IFRS will be identical. The UK Accounting Standards Endorsement Board is being established to endorse and adopt new or amended IFRS into the body of UK-adopted IFRS. The board is expected to be operational early in 2021.

80. The consolidated set of UK-adopted IFRS will be accessible on the UK board's website.

Thematic review on cash flow statements

81. The FRC has issued a report following their thematic review of cash flow statements. This was highlighted as an area requiring review due to the frequency of errors that had been identified. The objective of the thematic review was therefore to:

- explore in more detail the issues previously identified
- provide further guidance to avoid some of the more common errors.

82. The review found the following issues:

- material inconsistencies between items in the cash flow statement and the notes
- missing or incorrectly classified cash flows
- inconsistencies between financing cash flows and the reconciliation of changes in liabilities arising from financing activities in the notes.

Most of the errors were basic

83. Most of the errors were basic and evident from a desk top check. The appendix to the report provides more detail on each error. The FRC believes they could have been avoided by more robust checking prior to issue.

84. The review also identified several areas for improvement in the disclosure of accounting policies for the treatment of significant and large one-off transactions in the cash flow statement and the disclosures of related accounting policies and judgements.

Report on 2019/20 corporate reporting

85. The FRC has issued a report on the main findings arising from it monitoring of corporate reporting in 2019/20. It sets out:

- the current state of corporate reporting in the UK
- the main features of high quality reporting
- areas requiring improvement.

86. The report reminds entities that they need to meet the overarching objectives of accounting standards as well as their detailed disclosure requirements. This is particularly relevant where entities have to explain novel transactions or unusual circumstances, such as the effects of the COVID-19 pandemic.

87. Although COVID-19 has changed the context for corporate reporting, the key considerations of clarity, consistency, relevance and transparency remain. High quality disclosures:

- are specific to the entity
- explain clearly how COVID-19 has affected the reported financial position and performance, and how it may affect future prospects

Key reporting considerations remain despite COVID

- provide information on significant accounting judgements, sources of estimation uncertainty and other assumptions applied
- show a consistent outlook across the business model, principal risks and uncertainties, and accounting judgements and estimates.

88. The report highlights the main areas for improvement that have been identified. Those with potential relevance to the public sector are summarised in the following table:

Areas	How to address them
Estimates and judgements	Critical judgement disclosures should be tailored to each entity and not just repeat the accounting standard. They should explain the specific accounting judgements made and the effects. Sources of estimation uncertainty should be quantified. Information about sensitivities or ranges of outcomes should be disclosed to help users understand the effect of management's assumptions.
Impairment of assets	Entities which disclose significant judgements about whether to test assets for impairment need to explain the outcome of those judgements, the basis for the assumptions made and any sensitivities to changes in those assumptions.
Revenue from contracts with customers	When revenue is recognised over time, rather than at a point, entities should explain the basis for selecting this accounting policy. They should also explain the basis for monitoring how performance obligations are satisfied over time. Where entities have arrangements with multiple elements, they should explain any significant judgments made in identifying relevant performance obligations. Accounting policies should explain the nature of any variable consideration receivable and how it is estimated and constrained.
Financial instruments	Entities should give more information about liquidity risk.
Alternative performance measures (APMs)	Entities should not give undue prominence to APMs; for example, by only giving meaningful commentary on a non-GAAP (generally accepted accounting practice) basis. Reconciliations to GAAP measures should be given for all APMs, including ratios. Users should be able to relate reconciling items to GAAP measures in the accounts. Adjustments made in calculating APMs from IFRS amounts should include gains, as well as losses, when relevant to the definition of the APM.
Provisions and contingencies	Entities should disclose sufficient information to enable users to understand the nature of provisions, related uncertainties and the potential timing of cash outflows.
Fair value measurement	Fair value disclosures should be provided for all relevant areas of the financial statements, with explanations supporting judgements, and assumptions with sensitivity analyses where appropriate

Report on corporate governance reporting

89. The FRC has issued a report on corporate governance reporting in 2020. The report follows a review of the reporting by 100 companies of the UK Corporate Governance Code 2020.

Non-compliance with the code should be reported

90. The FRC's analysis found that companies who are not compliant with the governance code do not declare non-compliance; instead they include vague explanations and continue this pattern year on year.

91. The report advises that is it preferable to set out the approach to the entity's application of the code's principles, explain why this approach is appropriate for its individual circumstances and, if necessary, report the actions it has taken to mitigate the impact of not following the code.

92. The FRC expects entities to move away from boilerplate statements towards a more meaningful narrative. Use of examples is strongly encouraged, to demonstrate application of any non-compliance with the code.

93. To help navigation through the annual accounts and ensure cohesion with the corporate governance statement, entities should use signposting, linking different elements of the report, with clear reference to the code.

Discussion paper on a new corporate reporting framework

Principles-based framework for corporate reporting

94. The FRC has issued a discussion paper which contains proposals to develop a new principles-based framework for corporate reporting. It proposes a network of interconnected reports centred around a Business Report designed to facilitate better communication with a range of users.

95. The proposed network of reports is summarised in the following table:

Report	Purpose and content
Business Report	This report would be similar to a concise Strategic Report, but supported by a series of additional 'network reports'.
Network reports	These would be accessible on a standalone basis and could be a combination of 'mandatory' and 'voluntary' reports. The objective of an individual network report would drive its content, but there would be separate network reports for the full financial statements as well as, for example, corporate governance disclosures and sustainability reporting.
Public Interest Report	This new report would enable users to understand how the entity views its obligations in respect of the public interest, how it has measured its performance against those obligations and to provide information on future prospects in this area.

96. The proposed general principle for materiality is that it would be judged by reference to the communication objective of the specific report. A single definition of materiality as set out in accounting standards would not necessarily be appropriate for all reports.

97. It is proposed that there should be one common set of principles that apply to all reports. The principles would include those set out in the following table:

Principles	Explanation
System level attributes	The overarching qualitative characteristics that corporate reporting as a whole should possess.
Report level attributes	The overarching qualitative characteristics that an individual report should possess.
Content communication principles	The principles of effective communication, applied when preparing an individual report.

98. Comments should be sent to futurereporting@frc.org.uk by 5 February 2021

Contact point for this section

99. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Technical Bulletin 2020/4

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